No. 15915

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

In the Matter of the Properties
MOULIN ROUGE, INC., a corporation and successor in interest to MOULIN ROUGE, a limited partnership,
Bankrupt.

In the Matter of
MOULIN ROUGE, a Limited Partnership,
Bankrupt.

ROSEHEDGE CORPORATION, a corporation,
Appellant,

vs.

MILLIE STERETT,
Appellee.

APPELLANT'S OPENING BRIEF.

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Introductory Statement.

Rosehedge Corporation, a secured creditor, appeals from that portion of Paragraph III of that Order Confirming, Affirming and Approving Referee's Order Dated September 23, 1957, as Modified by the Court of the United States District Court for the District of Nevada rendered on Review by the Honorable John R. Ross, District Judge, and reading as follows:

> "* * * provided, however, that the Respondent, Rosehedge Corporation, shall deposit in that certain escrow hereinafter mentioned, and prior to the close thereof, a full Release of Chattel Mortgage of that certain Chattel Mortgage dated May 24, 1955, and executed by Alexander Bisno, a married man, and Louis Rubin, a married man, general partners, doing business as Moulin Rouge, a partnership, as Mortgagors, to Rosehedge Corporation, a California corporation, as Mort-

gagee, and recorded as Document No. 47539, in Book 56, Official Records, in the office of the County Recorder of Clark County, Nevada, and upon the close of said escrow, said Release of Chattel Mortgage shall be delivered to Petitioner, Millie Sterett. Such Release of Chattel Mortgage shall be without prejudice to the rights and claims of Rosehedge Corporation to interpose or assert any and all claims and defenses, except the claim of priority, to the validity and efficacy of the Chattel Mortgage dated July 5, 1955, and executed by Moulin Rouge, a Limited Partnership, Louis Rubin and Alexander Bisno, General Partners thereof, as Mortgagors, to Millie Sterett, as Mortgagee, and recorded July 13, 1955, as Document No. 51829, in Book 61, Official Records, and filed in File 19 in the office of the County Recorder of Clark County, Nevada" [R. 139-141].[1]

The Referee's Order Confirming Sale of Property Free and Clear of Liens, Excepting Certain Specified Liens Dated September 23, 1957, confirmed a sale made in open Court by the Referee on September 6, 1957, to one S. Kohn for $116,000.00 cash, and other payments. Said Order confirmed the sale of certain real property, free and clear of all taxes, liens and encumbrances, *excepting only:* (1) certain State, County and City taxes; (2) an assessment; (3) deed of trust executed by Edna Shulman, securing her $600,000.00 promissory note to Bisno & Bisno, Inc.; (4) assignment of said deed of trust by Bisno & Bisno, Inc., to Alexander Bisno and Louis Rubin; (5) assignment and pledge of the Shulman note and deed of trust by Bisno and Rubin to LeRoy Investment Co., Inc., to secure payment of their $250,000.00 promissory note; and (6) *assignment and pledge of the Shulman note and*

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[1]The Rosehedge Chattel Mortgage was recorded May 25, 1955 [R. 10-11, par. 11].

deed of trust by Bisno and Rubin to Rosehedge Corporation (subject to prior LeRoy assignment and pledge) to secure payment of a $195,000.00 promissory note by Moulin Rouge, a partnership, to Rosehedge Corporation. Referee's Order also confirmed the sale of Trustee's interest in furniture, furnishings, gaming equipment, and all other tangible personal property pertaining to the business of Moulin Rouge, *"subject, . . . to all valid and subsisting . . . chattel mortgages against the said personal property"* [R. 66-75].

The real property was purchased and sold subject to approximately $52,000.00 in taxes [R. 115]; the Leroy lien claim of $272,722.50 [R. 37-40]; the Rosehedge lien claim of $154,846.65 [R. 40-43]; and the Shulman note and trust deed of lien indebtedness of $427,569.15 [R. 41].

Trustee's interest in the personal property was purchased and sold "subject to all valid and subsisting . . . chattel mortgages." This includes a chatel mortgage held by Rosehedge Corporation, as additional security for its $195,000.00 promissory note, and the subsequent chattel mortgage held by Millie Sterett [R. 10-11, lines 11 and 13].

Several Reviews, including one by Alexander Bisno, for himself and on behalf of Millie Sterett [R. 75-81] were taken from the aforesaid Referee's Order. The District Judge's Order modified the Referee's Order pertaining to taxes (not involved upon this appeal [R. 133-134]; and as modified, affirmed the Referee's Order in all respects; it *expressly adjudged* that the sale of the real property to S. Kohn was a sale free and clear of all taxes, liens and encumbrances, *excepting only* taxes, as modified, and the various liens and lien claims as set forth in subparagraphs (2), (3), (4), (5) and (6) of the Referee's Order [R. 134-135]; (*subparagraph (6) is the lien and lien claim of Rosehedge Corporation*); it also dismissed the several Petitions for Review, and denied the relief sought

by the various Petitioners, except as otherwise provided in the Judge's Order [R. 135-137]; and provided for the payment of the increased purchase price through an escrow [R. 137-138]. The said Order, however, *further ordered Rosehedge Corporation to deposit in escrow, a full release of its chattel mortgage, for delivery to Millie Sterett, at the close thereof* [R. 136].

Rosehedge Corporation is aggrieved by this latter portion of said Order. It deprives it of the right to assert its superiority and priority, both in time and recordation, over the Sterett chattel mortgage. It permits Rosehedge to challenge the Sterett chattel mortgage solely for invalidity, or want of efficacy, other than the priority of its chattel mortgage over the Sterett chattel mortgage [R. 136].

This portion of the Judge's Order is based upon a claim first asserted by Sterett in her "Memorandum of Law" served and filed *at the hearing* upon Review—that the Rosehedge lien claim and chattel mortgage had been satisfied and extinguished by the bid of, and sale to S. Kohn, who made the bid in her name, but on behalf of LeRoy Investment Co., Inc., and Rosehedge Corporation. Yet the S. Kohn bid, *as made, expressly stated* [R. 31] that she offered to purchase the real property *subject, among others, to the Rosehedge lien and lien indebtedness,* and the Trustee's interest in the personal property *"subject to all valid chattel mortgages"* [R. 31]; the Referee's Order *expressly so confirmed* the sale [R. 72], and the District Judge's Order on Review *expressly confirmed, affirmed and approved the sale, as made* [R. 135]. The Sterett Petition for Review sets forth no grounds for review, or specification of error asserting the Referee's Order is erroneous because the Rosehedge indebtedness and its chattel mortgage was satisfied and extinguished by the bid of and sale to S. Kohn, or otherwise [R. 75-81]. No such question was presented for review by the Referee in his Certificate under "The Questions Presented" [R. 123].

No such issue was ever presented to, or raised before the Referee. No such finding or determination was ever made by the Referee. The "Memorandum of Law" cannot enlarge the scope of, or the grounds stated in, or the issues presented by the Petition for Review.

No further evidence was presented or introduced upon Review, before the District Judge, either to support such argument, or to sustain the challenged portion of the District Judge's Order. Until Alexander Bisno, for himself and on the behalf of Millie Sterett filed Petitions for Review from Referee's Orders of September 6, 1957, and September 23, 1957, respectively, Millie Sterett never appeared at, or participated in any hearing, meeting, proceeding or sale in these bankruptcy proceedings, except to file a claim; nor did she ever seek leave to foreclose her chattel mortgage, or file any petition for reclamation in these bankruptcy proceedings [R. 83]. Millie Sterett was *not* present, or represented at the sale. No bid was made, or objection interposed, on her behalf to the bid of, or sale to S. Kohn, at said sale, or thereafter, or to its confirmation at any time prior to September 23, 1957, when the Referee signed and filed his Order Confirming Sale. She has never made any showing that a better or higher bid could have been obtained [R. 82-84, 118-120, 131-132]. The Referee's Order expressly protects whatever rights she had, or has, as a chattel mortgagee lien claimant, since the personal property was sold to S. Kohn *"subject to all valid . . . chattel mortgages against said personal property"* [R. 73, 83, 119]. Millie Sterett was not a "person aggrieved" by such Order, and had no right of review therefrom [R. 120].

The present appeal relates solely to, and affects only the portion of the Order from which Appellant Rosehedge Corporation has appealed. Rosehedge Corporation is the Appellant, and Millie Sterett is the Appellee on this appeal.

Statement of Jurisdiction.

1. The statutory provisions believed to sustain the jurisdiction of the District Court are as follows: U.S.C.A., Title 11, Section 1, subdivision 10, providing that ". . . courts of bankruptcy shall include the District Courts of the United States. . . ." (Bankruptcy Act, Sec. 1, sub. 10);[2] U.S.C.A., Title 11, Section 11, subdivision (a), providing

> "The courts of the United States hereinbefore defined as courts of bankruptcy are hereby created courts of bankruptcy and are hereby invested, within their respective territorial limits . . . with such jurisdiction at law and in equity as will enable them to exercise original jurisdiction in proceedings under this title. . . ." (Bankruptcy Act, Sec. 2);

U.S.C.A., Title 11, Chapter 11, Sections 701 to 799, entitled, and providing for "Arrangements," meaning ". . . any plan of a debtor for the settlement, satisfaction, or extension of time of payment of his unsecured debts upon any terms; . . ." (Bankruptcy Act, Ch. XI, Secs. 301 to 399); U.S.C.A., Title 11, Section 110(f) ". . . real and personal property shall, when practicable, be sold subject to the approval of the Court . . ." (g) "The title to property of a bankrupt estate which has been sold shall be conveyed to the purchaser by the Trustee." (Bankruptcy Act, Sec. 70(f) and (g)); U.S.C.A., Title 11, Section 66, "Referees are hereby invested, subject always to a review by the judge, with jurisdiction to . . . (6) perform such of the duties as are by this title conferred on courts of bankrupcty, including those incidental to ancillary jurisdiction, as prescribed by rules or orders of the courts of bankruptcy of their respective districts . . ."

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[2]All references to the Bankruptcy Act refer to the Chandler Act, as amended.

(Bankruptcy Act, Sec. 38(6)); U.S.C.A., Title 11, Section 67(c), "A person aggrieved by an order of a referee may . . . file with the Referee a petition for review of such order by a judge . . ." (Bankruptcy Act, Sec. 39(c)).

2. The existence of jurisdiction of the District Court is shown by the following pleadings:

(a) Proceedings for Plan of Arrangement filed October 19, 1955, by Properties Moulin Rouge, Inc., a Nevada corporation, in the District Court of the United States for the District of Nevada, entitled "In the Matter of Properties Moulin Rouge, Inc., a corporation, and successor in interest to Moulin Rouge, a limited partnership, Debtor," No. 921 (new No. 55) [R. 91].

(b) Proceeding for Plan of Arrangement filed November 23, 1955, by Moulin Rouge, a Limited Partnership, in the District Court of the United States for the District of Nevada, entitled "In the Matter of Moulin Rouge, a Limited Partnership, Debtor," No. 925 (new No. 59) [R. 91].

(c) Order of reference whereby the aforementioned proceedings were referred to Referee John C. Mowbray [R. 89].

(d) Referee's Order on March 15, 1956, adjudicating Properties Moulin Rouge, a corporation, a bankrupt [R. 93].

(e) Referee's Order on April 12, 1956, adjudicating Moulin Rouge, a Limited Partnership, a bankrupt [R. 93].

(f) Petition of Trustee, filed May 21, 1956, to Sell Free and Clear of Liens, the property belonging to bankrupt estates, and Supplemental Petition thereto filed June 5, 1956 [R. 97-98].

(g) Petition of Trustee for Authority to Sell Property belonging to said estates, in accordance with the Bankruptcy Act [R. 98].

(h) Notice of Hearing on Petitions to Sell Real Property issued on June 5, 1956, and duly given to all creditors, attorneys, lienholders, lien claimants, and all parties in interest, setting hearing on June 18, 1956 [R. 98].

(i) Order to Show Cause Why Property Should Not Be Sold Free and Clear of Liens, filed June 5, 1956, and directed and given to all lienholders of record, and as listed in said Petition of May 21, 1956, and to creditors, and all persons in interest, setting hearing for June 18, 1956 [R. 98-99].

(j) Order for Sale of Property, and Order Authorizing Sale of Property Free and Clear of Liens, which authorized Trustee to sell, in accordance with the Bankruptcy Act, certain real property of the bankrupt estates, including all furniture, fixtures and other personal property contained therein *"upon such terms and conditions as the Court shall hereafter approve."* It also authorized Trustee to sell the same free and clear of the liens [R. 3-20, 103-105].

(k) Referee's Orders of Continuances of: Petition for Authority to Sell, the hearing thereon, the notices of hearings thereon, the notice of sale, and the sale, from time to time from June 18, 1956, finally to September 6, 1957 [R. 94, 105-110].

(l) The written bid of S. Kohn to purchase the real property, free and clear of all liens, claims and encumbrances, *except certain liens,* and Trustee's right, title and interest in and to certain enumerated personal property, *subject to all valid and subsisting conditional sales contracts and chattel mortgages against said personal property* [R. 29-39].

(m) Referee's Order Confirming Sale of Property Free and Clear of Liens Excepting Certain Specified Liens, dated September 23, 1957, confirming the sale of the real

and personal property, made in open Court, on September 6, 1957, to S. Kohn in accordance with terms of her bid [R. 66-73].

(n) Petition for Review of Referee's Order Confirming Sale of Property Free and Clear of Liens Excepting Certain Specified Liens, dated September 23, 1957, and filed on October 3, 1957, by Alexander Bisno, and on behalf of Millie Sterett [R. 75-81].

(o) The District Judge's Order Confirming, Affirming and Approving Referee's Order Dated September 23, 1957, as Modified by the Court, entered on November 9, 1957 [R. 128-139].

3. The statutory provisions believed to sustain the jurisdiction of the United States Court of Appeals for the Ninth Circuit are as follows: U.S.C.A., Title 11, Section 47, subdivision (a), providing "The Circuit Courts of Appeal of the United States . . . are hereby invested with appellate jurisdiction from the several courts of bankruptcy in their respective jurisdictions in proceedings in bankruptcy, either interlocutory or final, and in controversies arising in proceedings in bankruptcy, to review, affirm, revise or reverse both in matters of law and in matters of fact . . ." and subsection (b) thereof, providing "Such appellate jurisdiction shall be exercised by appeal and in the form and manner of an appeal." (Bankruptcy Act, Sec. 24(a) and (b)); U.S.C.A., Title 11, Section 48, subsection (a), providing "Appeals under this title to the Circuit Court of Appeals of the United States . . . shall be taken within thirty days after written notice to the aggrieved party of the entry of judgment, order or decree complained of . . . or if such notice be not served and filed, then within forty days from such entry." (Bankruptcy Act, Sec. 25a); U.S.C.A., Title 11, following Section 53, General Order 36 providing "Appeals shall be regulated, except as otherwise provided in the Act, by the

rules governing appeals in civil actions in the Courts of the United States, including the Rules of Civil Procedure for the District Courts of the United States"; U.S.C.A., Title 28, Federal Rules of Civil Procedure, Rule 73(a) "A party may appeal from a judgment by filing with the District Court a notice of appeal"; (b) "The notice of appeal . . . shall designate the judgment, *or the part thereof appealed from,* and shall name the Court to which the appeal is taken . . ." Rule 54a: " 'Judgment,' as used in these Rules, include any Order from Which an appeal lies. . . ."

4. The existence of jurisdiction of the United States Court of Appeals is shown by the following:

(a) The Order of the District Court Confirming, Affirming and Approving Referee's Order Dated September 23, 1957, as Modified by the Court, entered on November 9, 1957, which, in part, orders Rosehedge Corporation to release its chattel mortgage through escrow to Millie Sterett, holder of a subsequent chattel mortgage [R. 128-129].

(b) The Notice of Appeal timely filed by Rosehedge Corporation on December 12, 1957, from a specific and designated portion of the aforesaid Order of the District Court [R. 139-141].

Statement of the Case.

A. Statement of Facts.

On July 9, 1954, Edna Shulman, for valuable consideration, executed her promissory note to Bisno & Bisno, Inc., a Nevada corporation, for $600,000.00, with interest thereon at 6 per cent per anum from December 1, 1954. Both principal and interest were payable in installments as therein specified. This note was secured by a deed of trust, dated July 9, 1954, executed by Edna Shulman, trustor, to Pioneer Title Insurance and Trust Company,

Trustee, and Bisno & Bisno, Inc., Beneficiary, upon certain real property subsequently sold to S. Kohn. This deed of trust was recorded in Clark County, Nevada, on July 12, 1954 [R. 44-45, 95]. Subsequently this trust deed (and Shulman note) was assigned by Bisno & Bisno, Inc., to Alexander Bisno and Louis Rubin [R. 30, par. 4]. On or about April 27, 1955, Alexander Bisno and Louis Rubin executed their promissory note, to evidence a loan made to them by LeRoy Investment Co., Inc., a California corporation (hereinafter designated LeRoy) for $250,000.00, payable on or before August 27, 1955, with interest at 11½ per cent per annum. This note was secured by an assignment and pledge agreement, and a pledge of the aforementioned Shulman note and deed of trust. This assignment and pledge agreement was recorded in Clark County, Nevada, on April 29, 1955 [R. 38-40]. On or about May 24, 1954, Moulin Rouge, a partnership, and Louis Rubin and Alexander Bisno, as partners thereof, and individually, executed their promissory note to Rosehedge Corporation, a California corporation (hereinafter designated Rosehedge) for $195,000.00 to evidence a loan of said sum, with interest thereon at 6 per cent per annum; principal and interest were payable in weekly installments. This note was secured by an assignment and pledge agreement, and pledge (subject to the LeRoy assignment and pledge) of the aforementioned Shulman note and deed of trust, and *also* by a chattel mortgage, dated May 24, 1955, executed by Alexander Bisno and Louis Rubin, general partners doing business as Moulin Rouge, a Partnership, as mortgagors, to Rosehedge, as mortgagee, covering certain personal property located in the Moulin Rouge Hotel. Both the chattel mortgage and the aforesaid assignment and pledge agreement were recorded in Clark County, Nevada, on May 25, 1955 [R. 10-11, par. 11, 41]. On or about July 5, 1955, Moulin Rouge, a Limited Partnership, by its general partners Alexander Bisno and Louis Rubin,

as mortgagors, executed a chattel mortgage to Millie Sterett, as mortgagee, to secure a promissory note for $35,000.00,with interest thereon at 12 per cent per anum. This chattel mortgage was recorded in Clark County, Nevada, on July 13, 1955 [R. 11-12, par. 13; 21-29; 140-141].

Thereafter various defaults occurred in the payment and performance of the Rosehedge and LeRoy promissory notes and Rosehedge and LeRoy commenced foreclosure sales of their respective pledges [R. 89-92].

On October 19, 1955, Chapter XI Proceedings were filed by Properties Moulin Rouge, Inc., a corporation, and successor in interest to Moulin Rouge, a Limited Partnership, in the United States District Court for the District of Nevada. On October 27, 1955, after notice, the Referee enjoined the foreclosure proceedings and sales of LeRoy and Rosehedge. This Order remained in effect until September 6, 1957.

On November 23, 1955, Moulin Rouge, a Limited Partnership, filed Chapter XI proceedings in the United States District Court for the District of Nevada. Harry E. Miller was appointed Receiver, in each of the Chapter XI proceedings, and after adjudications, was elected Trustee in each proceeding. On January 17, 1956, Rosehedge and LeRoy filed their written Motion for leave to proceed with their pledge foreclosures and sales. Written objections thereto were filed by the Receiver. Said Motion and Objections were set for hearing before the Referee, and were heard on March 12, 13, April 5, 27, 28, 29, May 1, 24 and June 13 and 14, 1956, and then was submitted by the Referee for decision [R. 91-92].

On May 21, 1956, Trustee filed a Petition for authority to sell, free and clear of liens, the property belonging to the Bankrupt Estates. On June 5, 1956, he filed a Supplemental Petition thereto, and also filed a Petition for Au-

thority to Sell, in accordance with the terms of the Bankruptcy Act, the property belonging to the Bankrupt Estates. Notice of Hearings of said Petitions were duly given by mail, to all creditors, lienholders, lien claimants, attorneys, and all parties in interest [R. 98-99].

On June 18, 1956, the continued first meeting of creditors, and the hearings upon the aforementioned Petitions were held before the Referee. Several objections were interposed to said Petitions. LeRoy and Rosehedge contended that they would be seriously prejudiced by the sale of this property unless a proposed Stipulation was acceptable to Trustee's Counsel and approved by the Referee, by which a sale of the real property, free and clear of liens, could be held, pending the determination of the LeRoy and Rosehedge Motion, upon condition that LeRoy and Rosehedge could bid at any such sale, and use the amount of their respective lien claims, in whole or in part, on account of any bids made by them, and, in whole or in part, on account of the purchase price, if they became purchasers. The hearings were continued to June 19, 1956 [R. 99-102].

A satisfactory Stipulation was agreed upon, and signed and filed. It was approved by the Referee on June 19, 1956, and by reference, became a part of the subsequent July 6, 1956, Order [R. 101-102]. This Stipulation [R. 57-66] covered many matters, but pertinent portions thereof, in effect provided that pending the final determination of the aforesaid LeRoy and Rosehedge Motion, the real property could be sold by Trustee, at public sale under the supervision, and with the approval of the Court, free and clear of liens, upon condition that such sale be without prejudice to the rights and liens of Rosehedge and LeRoy; that the property be expeditiously sold; that the liens of LeRoy and Rosehedge be transferred to the proceeds of sale with the same priorities as held by their liens; that LeRoy and Rosehedge, jointly or severally, may be bidders at the sale, and entitled to use their respective

lien claims, in whole or in part, on account of bids made by them, and on account of the purchase price, if they became the purchasers [R. 57-66, 102-104].

On June 19, 1956, the first meeting of creditors, the various hearings, the notices of hearings, the notice of sale, and the sale, and each of them, was continued to July 30, 1956 [R. 105].

On July 6, 1956, the Referee signed and filed an Order for Sale of Property and Order for Sale of Property Free and Clear of Liens [R. 3-20, 105-106]. This Order (1) overruled all objections to Trustee's Petitions; (2) approved and incorporated by reference, the aforesaid Rosehedge-LeRoy Stipulation; (3) authorized Trustee to sell the real and personal property of Bankrupts, in accordance with Bankruptcy Act *"upon such terms and conditions as the Court shall hereafter approve";* and (4) authorized Trustee to sell the property of Bankrupts, free and clear of liens [R. 3-20].

No Reviews were taken from this Order, and it became final [R. 131]. On July 13, 1956, Millie Sterett filed a Proof of Secured Claim [R. 21-28]. It has never been approved or rejected. The Referee ordered the sale, and notice of sale, the first meeting of creditors, the further hearings upon Trustee's Petitions, and Notice of Hearing thereon, continued from time to time, to wit: from June 18, 1956, to June 19, 1956; then to July 30, 1956; then to September 10, 1956; then to November 27, 1956; then to January 25, 1957; then to February 26, 1957; then to May 23, 1957; then to July 22, 1957; and then to September 6, 1957. These continuances were ordered by Referee to permit a more advantageous sale, or the adoption of a feasible plan of arrangement, and were necessary because, either no bid, or no adequate or substantial bid, was offered or received on these dates, or to permit the completion and presentation of suggested plans of arrange-

ment, which would have resulted advantageously to general creditors, none of which, however, materialized [R. 94, 106-110]. During said period, the sale, and notice thereof, was advertised extensively, both locally and nationally, in local and nationally well-known and widely circulated newspapers, on numerous occasions, and for extended periods of time, and by brochures, prepared and sent by Trustee throughout the United States to thousands of prospective bidders and purchasers and other interested persons [R. 68].

The sale on September 6, 1957, was conducted by the Referee in open Court. It was well attended by large numbers of people, creditors and other parties in interest. Millie Sterett was neither present or represented at said sale. No bid on her behalf was made, and no objection on her behalf (or by anyone) was interposed to the bid of or sale to S. Kohn, at said sale, or thereafter, or to its confirmation, either by Sterett, or by anyone, between the date of sale and September 23, 1957, when the Referee signed and filed his Order Confirming Sale [R. 110, 118, 119, 131-132].

On September 6, 1957, during the sale conducted by Referee, a written bid by, and in the name of S. Kohn (a secretary to Mr. Katz), but on behalf of LeRoy and Rosehedge, was announced, made and submitted to the Referee, and read aloud to all persons present. The bid was then ordered filed [R. 110-112]. This written bid, as announced and made, provided that S. Kohn offered to purchase: (A) all the real property, with its improvements for $116,000.00 cash, free and clear of all liens, claims and encumbrances, excepting the following: (1) specified State, County and City taxes; (2) a specified assessment; (3) the $600,000.00 Shulman trust deed; (4) the assignment thereof by Bisno & Bisno, Inc., to Alexander Bisno and Louis Rubin; (5) the assignment and pledge of aforesaid trust deed by Bisno and Rubin to

LeRoy; (6) the assignment and pledge of aforesaid trust deed by Bisno and Rubin to Rosehedge; and additionally, and for the same consideration, (B) all of Trustee's right, title and interest in and to the furniture, furnishings, gaming equipment of all kinds, and other tangible personal property pertaining to the business of Moulin Rouge, *subject to all valid and subsisting additional sales contracts and chattel mortgages against the said personal property;* that the sale was to be consummated through, and the purchase price was to be paid in an escrow; that Purchaser was to obtain a policy of title insurance guaranteeing title as set forth in said bid. Said bidder also orally offered to pay costs of escrow, and title insurance policy, and to prorate the utility and insurance costs [R. 29-33, 110-112].

The Referee then requested further bids. Thereupon a recess of the sale for about one hour was requested by a prospective bidder to enable him to discuss a proposed plan of arrangement with certain lienholders to ascertain if the same would be acceptable to them. No objection thereto was interposed and the sale was recessed until 1:30 o'clock P.M. of said day [R. 112-113].

When the sale reconvened, the proposed plan, as a bid, was submitted. Various objections thereto were interposed, discussed, and analyzed; it was disclosed that such bid was not a firm bid, but was incomplete, conditional, contingent, and dependent upon too many contingencies and uncertainties; that it would require a lengthy continuance, and the consents of all lienholders, without any assurance, or hope of success, that a feasible and acceptable plan could, or would be presented at a later date [R. 112-114].

The Referee then stated to all present that for two years he had sought primarily to assist the unsecured general creditors; that during such period he had restrained

secured creditors from proceeding with foreclosures; that the Trustee had used every effort to sell the assets without avail; various plans of arrangement had been proposed, but no feasible plan had been presented; that secured creditors could not be restrained forever; that the property was depreciating; that costs and expenses were rapidly mounting; that the Trustee's Report showed that approximately $52,000.00 of real estate taxes had accrued and were unpaid; that unpaid costs and expenses of preservation of assets incurred by Receiver and Trustee then exceeded $70,000.00, which with taxes were accumulating in excess of $6,000.00 per month; that costs of administration remained unpaid; that the property had been extensively advertised throughout the United States, yet no bid or offer had been received or submitted which could be accepted by the Referee; that the proposed plan was not a firm bid; it was too contingent and depended upon too many uncertainties; it required further delays and required the consent of all lienholders, which apparently was not forthcoming; that the time had come when he was compelled to stop the mounting expenses; that under the law and Bankruptcy Act, he could not delay the proceedings any longer. The Referee then rejected this bid. The bid of S. Kohn was then renewed, as previously made; the Referee asked for other bids, and there being none, the Referee then accepted the bid of S. Kohn, as made, as the highest and best bid made, and there being no objections thereto, directed Trustee's counsel to prepare and present for signature an appropriate Order confirming said sale to S. Kohn [R. 115-116].

After the sale, an escrow, as provided by the S. Kohn bid was opened, and is pending [R. 16].

Also, on September 6, 1957, the Referee rendered his decision on the LeRoy and Rosehedge Motion; he granted said Motion; overruled the Trustee's Objections thereto, upheld the validity and lien of the LeRoy and Rosehedge

pledges, and announced the amounts thereof, and upheld the validity and lien of the Shulman trust deed and validity of the Shulman note [R. 33-48, 84-88]. On said date, *after the sale,* the Referee signed and filed his Order in respect thereto. This Order [R. 33-48] among other things, provides (1) that the LeRoy and Rosehedge Motion was granted; (2) that Trustee's objections thereto were overruled; (3) that there was a total sum of $272,722.50 due, owing and unpaid to LeRoy upon its promissory note which was secured by the valid first pledge of the Shulman note and trust deed; (4) that there was a total sum of $154,846.65 due, owing and unpaid to Rosehedge upon its promissory note which was secured by a valid pledge of the Shulman note and trust deed, subject to the prior LeRoy pledge; (5) that the Shulman note was valid and supported by adequate and legal consideration, without any infirmities or defenses thereto, and was secured by a valid trust deed, creating a valid first lien upon the real property described therein; and that the amount due and owing upon the Shulman note was the total amount due and owing to LeRoy and Rosehedge. Other portions of said Order provided for certain priorities; that the real property be offered for sale by the Court, and the liens of LeRoy and Rosehedge be transferred to the proceeds of sale; that if no such sale were made, LeRoy and Rosehedge then were authorized to proceed with their foreclosure sales [R. 33-48].

Several Petitions for Review, including one by Alexander Bisno, for himself and on behalf of Millie Sterett, were taken from Referee's Order, dated September 6, 1957 [R. 50-66] and were denied by the District Court. This Order has become final.

On September 23, 1957, the Order Confirming Sale of Property Free and Clear of Liens, Excepting Certain Specified Liens was signed and filed by the Referee [R. 66-75, 116]. This Order [R. 66-75] among other things,

confirmed the sale to S. Kohn for $116,000.00 cash of the real property, free and clear of all taxes, liens and encumbrances, except only the following: (a) specified State, County and City taxes; (b) a specified assessment; (c) the $600,000.00 Shulman trust deed; (d) assignment of aforesaid trust deed by Bisno & Bisno, Inc., to Alexander Bisno and Louis Rubin; (e) assignment and pledge of aforesaid trust deed by Bisno and Rubin to LeRoy; and (f) *assignment and pledge of aforesaid trust deed by Bisno and Rubin to Rosehedge,* together with the sale to S. Kohn of the Trustee's interest in the personal property *"subject to all valid and subsisting . . . chattel mortgages against the said personal property"* as made on September 6, 1957, and directed Trustee to execute proper instruments of conveyance of the said real and personal property, subject to the items, as aforesaid, upon the payment of the purchase price [R. 66-75].

On October 3, 1957, Alexander Bisno, for himself, and on behalf of Millie Sterett, filed a Petition for Review from the aforementioned Order Confirming Sale [R. 75-81]. This Petition set forth the following grounds of review: (1) That on July 6, 1956, the Referee authorized the sale of the real property free and clear of all liens; that the offer of and sale to S. Kohn was contrary to, and not in accordance with such Order, but was made expressly subject to the Shulman $600,000.00 trust deed and the assignments thereof to LeRoy and Rosehedge; that notice, as required by the Bankruptcy Act was not given with reference to the sale to S. Kohn; (2) that the evidence was not sufficient to justify said Order in that (a) the Shulman note and trust deed never were valid, and that LeRoy and Rosehedge were not lawful holders, owners, pledgees or pledge holders of the same; (b) that there were prior and superior rights than those asserted by said corporation (no specifications thereof); (c) that the Shulman note was not valid or supported by adequate or legal

consideration (no specifications thereof); (d) that neither of said corporations were *bona fide* purchasers of the Shulman note; (e) that neither of said corporations took said note in good faith, or for value; (f) that both corporations had actual notice or knowledge of infirmities in said note, and the taking thereof amounted to bad faith; (g) that the September 6, 1957, Order provides that if the real property be sold, the lien and claims of LeRoy and Rosehedge be transferred to the proceeds of sale, but if the property be not sold, then LeRoy and Rosehedge are authorized to proceed with a foreclosure sale, and that the offer of and sale to S. Kohn was subject to trust deeds and was contrary to the July 6, 1956, Order, and July 19, 1956, Stipulation and September 6, 1957, Order, and was made without notice to creditors, or interested parties; (h) that, upon information and belief, the Order of September 6, 1957, was the result of a compromise, and that no notice of compromise was given to creditors; (i) irregularities in proceedings which prevented Petitioner from having a fair trial (no specifications); (j) accident and surprise (no specifications); (k) newly discovered evidence (no specifications); (l) error in law occurring at the hearing and excepted to by the parties injured by said Order (no specifications); (3) the Petition for Review of Referee's Order of September 6, 1957, also was incorporated by reference. The prayer asked that the Order of September 23, 1957, be reversed, and that its execution or enforcement be stayed [R. 75-81].

This Petition for Review does not set forth therein, as a ground of review, or otherwise specify as error, that the Referee's Order incorrectly determined her asserted claim that the Rosehedge lien claim and its chattel mortgage was extinguished and satisfied by the bid of and sale to S. Kohn. The Petition *expressly alleges the contrary, i. e.,* that the sale to S. Kohn was made *subject to the LeRoy and Rosehedge liens,* and therefore, is *not in accord with, and contrary to the July 6, 1956, Order* [R. 76-78].

Except for two specifications of grounds for review (subparagraph a of paragraph 7 [R. 78] and part c. of subdivision 6 of subparagraph b of paragraph 7 [R. 77-78]) most of the grounds of review are directed to Referee's Order of September 6, 1957 (the subject of a separate review), and were filed too late to review that Order, and seek to collaterally attack it. The only grounds directed to the September 23, 1957 Order assert that the bid of and sale to S. Kohn violated the Order of July 6, 1956, an untenable position rejected by the District Court.

There was no adversary, or other proceedings, between Rosehedge and Millie Sterett, before the Referee, either during the sale, or thereafter, prior to the Referee's Order Confirming Sale, dated September 23, 1957, which involved or litigated any question of priority of their respective chattel mortgages, or any question of the extinguishment or satisfaction of the Rosehedge lien claim and chattel mortgage. On the contrary, Millie Sterett was not present or represented at said sale, nor did she file any exceptions or objections thereto, or to its confirmation at any time prior to its confirmation [R. 117, 119, 131-132]; Referee's Order Confirming Sale does not determine, include, or involve any such issues.

The several Petitions for Review were heard by the District Judge on October 28, 1957. At this hearing, counsel for Millie Sterett served and filed a "Joinder of Millie Sterett in Petitions for Review," asserting for the *first time* that A. Bisno had been authorized to sign on her behalf the aforementioned Petitions for Review from Referee's Orders of September 6, 1957, and September 23, 1957, respectively, and stated therein that *"Millie Sterett hereby personally joins in said Petitions for Review"* [R. 127]. Also at this hearing Counsel for Millie Sterett served and filed a "Memorandum of Law in Support of

Petition for Review of Referee's Order of September 23, 1957," wherein she urged *for the first time,* that the lien claim of Rosehedge has been satisfied by utilizing the full amount thereof in the bid of S. Kohn at the sale, and extinguishing its chattel mortgage, and based such argument upon an isolated portion of the Referee's Certificate [R. 117-118]. The Referee therein *expressly stated* that the bid of S. Kohn was made *subject to the lien and claims of LeRoy and Rosehedge,* and to show that such bid was not prejudicial to the Bankrupt Estates, or to Trustee, the Referee, stated, *by way of illustration only,* that *in his opinion* such a bid was the *equivalent* of a bid which would have utilized the value of the LeRoy and Rosehedge claims, for had such a bid been made, the amount thereof increased by the utilization of the value of the LeRoy and Rosehedge claims, would have resulted in a credit upon the purchase price in the amount of the value of such claims, thus leaving the *net amount* of the purchase price received by the Bankrupt Estates and the Trustee, upon such a bid, in the same amount as that received by the Bankrupt Estates, and the Trustee, by the bid of and sale to S. Kohn, subject to such liens and lien claims. The Referee did not, by such illustration, state, find or determine that the bid of S. Kohn did utilize the value of the LeRoy and Rosehedge claims. He stated the *contrary.*

Both the Referee's Order Confirming Sale, and the District Judge's Order, directly contradict Millie Sterett's contention. The Referee's Order expressly confirms the sale of the property, *subject to the Rosehedge lien claim,* and the personal property, *subject to chattel mortgages* [R. 72, par. 6; 73]; the District Judge's Order confirmed the sale as made by the Referee, and adjudicated that the sale was one *subject to the Rosehedge lien claim* [R. 134-135]. There was no evidence offered or introduced before the Referee that the lien claims of LeRoy and Rosehedge had been utilized by the bid of S. Kohn. The terms of the bid

are to the contrary; no such evidence was offered or introduced before the District Judge on review.

The District Judge's Order Confirming, Affirming and Approving Referee's Order Dated September 23, 1957, as Modified by the Court was signed and filed on November 7, 1957, and entered on November 9, 1957. This Order [R. 128-139] modified the Referee's Order pertaining to taxes (not involved upon this appeal) [R. 133-134]; and as modified, affirmed the Referee's Order in all respects; it *expressly adjudged* the sale of the *real* property to S. Kohn to be a sale free and clear of all taxes, liens and encumbrances, *excepting only* the taxes, as modified, and the various liens as set forth in subparagraphs (2), (3), (4), (5) and (6) of the Referee's Order [R. 134-135]; (*subparagraph (6) is the lien indebtedness of Rosehedge*) it dismissed the several Petitions for Review, and denied the relief sought by the Petitioners, except as otherwise therein provided [R. 135-137]; and provided for the payment of the increased purchase price through an escrow [R. 137-138]. The said Order, however, *further ordered* Rosehedge to deposit a full release of its chattel mortgage in said escrow for delivery at the close thereof to Millie Sterett, a subsequent mortgagee [R. 136].

On December 12, 1957, Rosehedge timely filed a Notice of Appeal from that portion of the District Court's Order whereby Rosehedge was ordered to deposit in escrow a full release of its chattel mortgage, for delivery, upon the close thereof, to Millie Sterett [R. 139-141]. All other portions of said Order have become final. Rosehedge also filed an Undertaking for Costs on Appeal [R. 141-143].

B. Questions Involved.

1. Did the District Court err in ordering Rosehedge to deposit a full release of its chattel mortgage in escrow for delivery upon the close thereof to Millie Sterett, a subsequent chattel mortgagee, upon the record before the Dis-

trict Court upon Review from Referee's Order[3] which confirmed the sale of encumbered personal property *subject to all chattel mortgages?*

2. Did the District Court upon Review from Referee's Order err in holding that Millie Sterett, a chattel mortgagee was a "person agrieved" by Referee's Order which confirmed sale of encumbered personal property *subject to all chattel mortgages?*

3. Did the District Court upon Review from Referee's Order err in ordering Rosehedge to release its chattel mortgage, as aforesaid, in that the Sterett Petition for Review does not set forth any grounds for review, or any specification of error, specifying that Referee's Order erroneously determined her asserted claim that the bid of and sale to S. Kohn of the property, subject to specified liens (including Rosehedge lien) and all chattel mortgages, satisfied and extinguished the Rosehedge lien claim and its chattel mortgage?

4. Did the District Court upon Review from Referee's Order have jurisdiction to determine the question of the rights and priorities between Rosehedge and Sterett as to their respective chattel mortgages where the encumbered property had been sold to a third person subject to all chattel mortgages, and neither Trustee or the Bankrupt Estate had any interest in such controversy?

5. Did the District Court upon Review from Referee's Order err in ordering Rosehedge to release its chattel mortgage, as aforesaid, where no issue that the Rosehedge lien claim was satisfied, or its chattel mortgage extinguished by the bid of, and sale to S. Kohn, was ever raised or interposed before, or determined by, the Referee

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[3]Referee's Order, as used herein, refers to Referee's Order Confirming Sale of Property Free and Clear of Lien Except Certain Specified Liens, dated September 23, 1957.

at or after the sale, and where no adversary proceedings between Rosehedge *and* Sterett upon such issue was ever held before or heard by the Referee, and no evidence upon such issue was introduced before the Referee, or upon Review before the District Judge?

6. Did the District Court upon Review from Referee's Order which confirmed sale of encumbered personal property *subject to all chattel mortgages* err in determining the question of the rights and priorities between Rosehedge and Sterett as to their respective chattel mortgages, under the circumstances set forth in preceding Question No. 5, thereby depriving Rosehedge of its day in Court, upon the merits of such issue or question, or should the District Court have required the parties to seek a determination of such rights and priorities in an appropriate proceeding before the proper forum—the State Courts.

7. Did the District Court, upon Review from Referee's Order, err in holding that, *as a matter of law,* the bid of and sale to S. Kohn, acting on behalf of LeRoy and Rosehedge, satisfied the lien claim of Rosehedge and extinguished its chattel mortgage as against Millie Sterett, a subsequent chattel mortgagee, who was not present or represented at such sale, and filed no objections thereto, or to the confirmation thereof, at any time prior to its confirmation, and who never urged such contention before the Referee?

8. Did the District Court, upon Review from Referee's Order, err in failing to dismiss the Sterett Petition for Review without relief to her, in that she was estopped from reviewing such order for failure to make timely objections thereto where she was not present or represented at said sale, after notice thereof, and made no objection to the bid, sale, or its confirmation thereat, and filed no objections thereto, or to the confirmation thereof, at any time prior to September 23, 1957, when Referee's Order was signed and filed?

9. Is the portion of the District Court's Order ordering Rosehedge to release its chattel mortgage to Sterett, as therein provided, supported by the evidence?

10. Is the portion of the District Court's Order ordering Rosehedge to release its chattel mortgage, to Sterett, as therein provided, contrary to the evidence?

11. Is the portion of the District Court's Order ordering Rosehedge to release its chattel mortgage, to Sterett, as therein provided, contrary to law for each and all of the reasons hereinbefore stated?

Specifications of Errors.

1. The District Court, upon Review from Referee's Order[4] prejudicially erred in rendering that portion of its Order whereby Rosehedge was ordered to deposit a full release of its chattel mortgage in escrow for delivery upon the close thereof to Millie Sterett, a subsequent chattel mortgage claimant upon the grounds and for the reasons hereinafter specified.

2. The District Court, upon Review from Referee's Order, prejudicialy erred in ordering Rosehedge to release its chattel mortgage through escrow to Millie Sterett, a subsequent chattel mortgagee, in that Millie Sterett was not a "person aggrieved" by Referee's Order which confirmed sale of encumbered personal property *subject to all chattel mortgages,* thereby fully protecting and preserving her right as a chattel mortgagee.

The bid of S. Kohn provided for the purchase of Trustee's interest in the personal property, *subject to all chattel mortgages* [R. 31] and it was so accepted [R. 110-112, 116, 119-120]. The Referee's Order [R. 66-74] confirm-

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[4]Referee's Order refers to Referee's Order Confirming Sale of Property Free and Clear of Liens, Excepting Certain Specified Liens dated September 23, 1957 [R. 66-75].

ing such sale "subject . . . to all valid . . . chattel mortgages . . ." [R. 73]. The Judge's Order confirmed the Referee's Sale, as made, except for taxes [R. 134-135]. The Referee's Certificate [R. 119] states: "The Order Confirming Sale expressly protects her (Millie Sterett's) rights as a chattel mortgage lien claimant. It provides that said personal property was sold 'subject to all valid and subsisting conditional sales contracts and chattel mortgages against said personal property.' Whatever rights she may have in respect to her chattel mortgage, such rights are expressly preserved to her under the Order Confirming Sale" [also R. 83].

Under U.S.C.A., Title 11, Section 67c (Sec. 39c, Bankruptcy Act) Millie Sterett was not a "person aggrieved" by Referee's Order. The Referee's Certificate so states [R. 120, 84].

3. The District Court, upon Review from Referee's Order, prejudicially erred in ordering Rosehedge to release its chattel mortgage through escrow to Millie Sterett, in that the Sterett Petition for Review does not set forth any grounds of Review, or specification of error, specifying that Referee's Order erroneously determined her asserted claim that the bid of, and sale to S. Kohn satisfied and extinguished the Rosehedge lien claim and chattel mortgage, or even makes any reference thereto. Such contention was first asserted by Sterett in her "Memorandum of Law," at the hearing on Review.

There is *nothing* in the Petition for Review [R. 75-81] to the effect that sale to S. Kohn satisfied or extinguished the Rosehedge lien claim and its chattel mortgage, either as grounds for review, specification of error, or otherwise. On the contrary, Petitioner alleges that the offer of and sale to S. Kohn was *not free and clear, but was subject to liens* [R. 76-77, 78]. Certain of her specifications are directed to the sale of the real property, assert-

ing that it violated prior Orders; other specifications are directed to *Referee's Order dated September 6, 1957,* which granted the LeRoy and Rosehedge Motion, which involved the *real property only.* (These specifications came too late.) Such Order does not affect, relate to, or involve the Sterett chattel mortgage [R. 33-48, 83, 95-96]. The claim that the Rosehedge lien claim and chattel mortgage was satisfied and extinguished was *first asserted* in Sterett's "Memorandum of Law" served and filed *at the hearing* upon Review [R. 124-126]. This "Memorandum" cannot enlarge the scope of, or add to the Petition for Review.

4. The District Court, on Review from Referee's Order, prejudicially erred in ordering Rosehedge to release its chattel mortgage to Millie Sterett through escrow in that no issue or claim that the Rosehedge lien claim and chattel mortgage was satisfied and extinguished by the sale to S. Kohn was raised, interposed or presented before or determined by Referee at the sale, or thereafter; no adversary proceedings between Rosehedge and Sterett upon such issue ever was initiated or held before the Referee, and no evidence upon such issue was introduced before the Referee, or on Review before the District Judge.

Millie Sterett was given notice of sale [R. 119, 122, 132]; she was not present or represented at the sale; no objection to the bid of, or sale to S. Kohn was interposed at said sale; no objection on her behalf to the S. Kohn bid, or sale, or to the confirmation, was interposed thereat, or thereafter, prior to Referee's Order, signed and filed on September 23, 1957; no issue was raised, or claim was presented by Sterett, that the Rosehedge lien claim and its chattel mortgage, had been extinguished by the said bid and sale, at any time prior to the hearing on Review [R. 82-84, 110, 117, 119]; no hearing was had, or any evidence was ever introduced on that issue; the District

Court's Order also states the foregoing facts [R. 131-132].

5. The District Court upon Review from Referee's Order prejudicially erred in summarily determining the rights and priorities, between Rosehedge and Sterett as to their respective chattel mortgages, without any hearing thereon, or presentation of any evidence upon such issue, thereby depriving Rosehedge of its day in Court upon the merits of such issues. The District Court should have required Sterett to have such issues determined in appropriate proceedings, in the State Courts, since such issues were governed by State law.

(See references to record, and statements in respect thereto, set forth under Specification No. 4.)

6. The District Court upon Review from Referee's Order prejudicially erred in summarily determining the rights and priorities between Rosehedge and Sterett, as to their respective chattel mortgages, upon property sold to a third person subject to chattel mortgages, as the Bankruptcy Court did not have general jurisdiction to hear controversies between adverse third persons, which are not strictly and properly part of bankruptcy proceedings and not a necessary incidental to administration of bankrupt estates, and neither Trustee nor bankrupt estates had any interest in such controversy?

(See references to record and statements in respect thereto set forth under Specification No. 4.)

The controversy raised by Millie Sterett for the first time at the Review hearing [see Memorandum of Law, R. 124-126] was one *solely* between Sterett and Rosehedge. It was an irrelevant, ancillary and collateral matter so far as the administration of the bankrupt estates were concerned, since the sale of the personal property, subject to all chattel mortgages, preserved all of Sterett's

rights and remedies as a chattel mortgagee. It was not a necessary incidental to the administration of the bankrupt estates, and one in which neither Trustee nor Bankrupt Estates had any interest, and the Bankruptcy Court had no jurisdiction to determine such controversy.

7. The District Court upon Review from Referee's Order prejudicially erred in ruling, *as a matter of law,* that the bid of and sale to S. Kohn, on behalf of LeRoy and Rosehedge, satisfied and extinguished the Rosehedge lien claim and chattel mortgage, in favor of Millie Sterett, a subsequent chattel mortgagee, who was not present or represented at such sale, and filed no objection thereto, or to the confirmation thereof, at any time prior to signing and filing of Referee's Order.

(See references to record, and statements in respect thereto, set forth under Specifications Nos. 2 and 4.)

8. The District Court upon Review from Referee's Order prejudicially erred in failing to dismiss the Sterett Petition for Review without relief in that she was estopped from reviewing such Order for failure to make timely objection thereto, where she was not present or represented at the sale, after notice thereof; and no objection to the bid or sale was made thereat; she filed no objection or exception thereto, or to the confirmation thereof, at any time prior to the signing and filing of said Referee's Order.

(See references to record and statements in respect thereto set forth under Specification No. 4 hereof.)

9. The portion of the District Court's Order ordering Rosehedge to release its chattel mortgage through escrow to Millie Sterett, a subsequent chattel mortgage claimant, is prejudicially erroneous in that it is not supported by the evidence.

The evidence is as follows:

Referee's Order [R. 66-74] recites the facts occurring and the proceedings had on September 6, 1957, at the sale, and contains the Referee's "informal findings" in respect thereto. This Order states that notice of sale was given to all creditors, lien holders, lien claimants, attorneys and all interested parties, and had been extensively advertised. That at the sale S. Kohn made an offer in open Court to purchase the real property, free and clear of liens, *except certain specified liens,* together with Trustee's right, title, and interest in certain personal property "subject . . . to all valid . . . chattel mortgages" for $116,000.00 *cash,* payable through an escrow to be opened; that other bids were received; that the bid of S. Kohn was the highest and best bid made, and which could be obtained, and that the Court accepted the S. Kohn bid, *as made;* that said sale in all respects was regular; and in accordance with Orders of Court and provisions of Bankruptcy Act, and that it was in the best interests of the Bankrupt Estates; and that there was no opposition to said bid, sale, or its confirmation [R. 67-70].

The District Court's Order on Review [R. 128-139] states among other things, "that the statement of facts and the recital of the proceedings had, as set forth in the aforementioned Referee's Order, dated September 23, 1957, *are correct,* and by reference made a part hereof" [R. 130]; that each Petitioner on Review were given and received due notice of all proceedings; that the July 6, 1956, Order had become final; that due notice of the time and place of sale had been given to all creditors, lienholders, lien claimants, attorneys and other interested parties including all Petitioners on Review (Sterett) as required by law and the Bankruptcy Act, and to the general public; that Sterett was not present or represented at the sale; that no objection to the bid of, or sale to S. Kohn, or to

its confirmation, was made at the sale, or thereafter at any time prior to its confirmation by or on behalf of any Petitioner on Review, or by anyone; that no showing has been made by anyone that a better or higher bid, offer, or sale, could be had; that said sale complied with the Orders of Court; that the S. Kohn bid was made on behalf of LeRoy and Rosehedge; that the bid of S. Kohn was the highest and best bid made, and received at said sale, and the highest and best bid that could have been obtained for the property; that the Referee's sale was a public sale, legally made and fairly and impartially conducted and in all respects regular and in accordance with the Orders of Court and the Bankruptcy Act; and that said sale was in the best interests of the Bankrupt Estates [R. 130-132].

There is no recital, statement or finding in either the Referee's Order, or in the District Court's Order upon Review, that the bid of or sale to S. Kohn used, utilized, or included the value of the LeRoy and Rosehedge claims, or that said sale satisfied and extinguished the Rosehedge lien claim, and its chattel mortgage. There is no such evidence!

The *undisputed* evidence further shows that S. Kohn, on behalf of LeRoy and Rosehedge, made a written bid by which she offered to purchase the real property, *subject to certain liens, which included the Rosehedge lien,* and Trustee's interest in the personal property, *subject to all valid chattel mortgages,* for $116,000.00 *cash* [R. 29-33, 110-112]. This bid was accepted, *as made,* and the property was sold to S. Kohn *in accordance* with the bid [R. 110-112, 116, 120-121]. The Referee's Order [R. 66-74] confirmed the sale as provided by the bid [R. 66-74, 90, 116, 120-121]. The District Court's Order affirmed the sale as made by Referee, with a modification of taxes [R. 134-135]. On September 6, 1957, the LeRoy lien claim was $272,722.50 [R. 37-38], and the Rosehedge lien claim

was $154,846.65 [R. 40-42, 84-87].[5] The S. Kohn bid was for $116,000.00 *cash* for the real and personal property, subject to various liens and chattel mortgages [R. 29, 69, 90, 111]; this was increased to $117,500.00 *cash* before the District Judge [R. 130, 137-138]; and the sale was confirmed for $116,000.00 and $117,500.00 *cash,* respectively, subject to specified liens and all valid chattel mortgages.

Obviously, the aforesaid cash bid and purchase price did not include or utilize the value of the LeRoy and Rosehedge claims ($427,569.15) since said claims were far in *excess of the actual bid and purchase price.* Nothing can be read into the record which did not exist, and which did not take place.

The Referee's *expression of opinion* [R. 124-126], used by way of illustration, that the bid by S. Kohn, subject to the liens and claims of LeRoy and Rosehedge, *in his opinion,* was the *equivalent* of utilizing the value of LeRoy and Rosehedge claims, is *not evidence,* and cannot support the portion of the Order from which Rosehedge has appealed. This expression is purely gratuitous; it is *not* a finding of fact (it was made long after Referee's Order was filed); it is not a *recital* of the facts which *occurred* at the sale (see Referee's Order); it is but an *expression of opinion* by the Referee, made *long after* the sale, and *subsequent* to the signing and the filing of the Referee's Order (it cannot impeach such Order); *it was used, by Referee, by way of illustration only,* to demonstrate that no prejudice resulted to the Bankrupt Estate, or the Trustee from the bid of and sale to S. Kohn, as made, subject to liens and chattel mortgages, for insofar as *net results*

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[5]Referee's Certificate on Review from Referee's Order of September 23, 1957, incorporates by reference Referee's Certificate on Review from Referee's Order of September 6, 1957 [R. 91, 92, 119].

to the Bankrupt Estates, and the *net amount* of money received by the Trustee, were concerned [R. 120], the Kohn bid, *in the opinion of the Referee,* was the *equivalent* of a bid which would have utilized the value of the LeRoy and Rosehedge lien claims. While such a bid would have been increased by the value of such lien claims, when accepted, would have necessitated the giving of a credit for the value of such lien claims upon the purchase price, leaving the *net result* for the Bankrupt Estates, and the *net amount of money* received by the Trustee, from such bid, the *same* as that received from the bid of and sale to S. Kohn [R. 120]. That was the sole reason for the Referee's statement. The Referee did not thereby, or therein, state, or find, that the bid of S. Kohn, in fact, had included, or had utilized the value of the LeRoy and Rosehedge claims, or that it satisfied or extinguished the Rosehedge chattel mortgage. No such issue or question was then presented to or before the Referee. This is further illustrated by the "Status of Record" in Referee's Certificate [R. 121-123], wherein the evidence is summarized, and no reference is made to any utilization of the value of the Rosehedge claim in the S. Kohn bid; by Referee's statement that the Kohn bid, as made, subject to liens, was more beneficial to the Bankrupt Estates, since no part of the proceeds of sale could be charged with taxes [R. 120], and that the sale to S. Kohn, *as made,* did comply with that portion of the July 6, 1956 Order [par. 3, R. 6-7], which authorized the sale of the real property including the furniture, fixtures and other personal property contained therein, *"upon such terms and conditions as the Court shall hereafter approve"* [R. 120], which is severable, separate and distinct from the other portion of said Order (par. 4) which also authorized Trustee to sell the property free and clear of liens. The Trustee could sell under *either* provision.

The record is totally devoid of any evidence which shows that there was any announcement made at the sale that the Kohn bid included or utilized the value of the LeRoy and Rosehedge claims, or that it was so intended. The actual announcement made at the sale [R. 110-112] and the written bid submitted, filed and accepted thereat is directly to the contrary [R. 29-33, 111-112, 116].

10. The portion of the District Judge's Order upon Review ordering Rosehedge to release its chattel mortgage through escrow to Millie Sterett, a subsequent chattel mortgage claimant, is erroneous in that it is contrary to the evidence and to the recital of facts stated in both Referee's Order and District Court's Order.

The substance of evidence; the several references to the Record, and various statements made in connection therewith, as set forth under Specification No. 9, are equally applicable to this Specification, and are made a part hereof by reference.

11. That portion of the District Court's Order upon Review ordering Rosehedge to release its chattel mortgage through escrow to Millie Sterett, subsequent mortgage claimant, is prejudicially erroneous in that it is not supported by, and is contrary to law, for the reasons, and upon the grounds hereinbefore specified.

Summary of Argument.

The headings on our argument have been prepared so that they may serve as a summary. Accordingly, we incorporate by reference the index of the argument appearing at the commencement of this brief as the summary of the argument, and respectfully direct this Honorable Court's attention thereto.

ARGUMENT—POINTS AND AUTHORITIES.

I.

The District Court Upon Review, Prejudicially Erred in Ordering Appellant to Release Its Chattel Mortgage Through Escrow to Appellee Since Appellee Was Not "Party Aggrieved" by Referee's Order, and Was Not Entitled to Review the Same.

Sterett's Petition for Review alleges that she is a secured creditor holding a chattel mortgage upon personal property listed therein [R. 75, 82]. Her sole interest in the bankruptcy was that of a subsequent chattel mortgagee upon the personal property sold by Referee to S. Kohn, *subject to all valid chattel mortgages.* The Referee's Order [R. 66-74] confirmed the sale of Trustee's interest in the personal property "subject . . . to all valid . . . chattel mortgages" [R. 73].

U.S.C.A., Title 11, Section 67c (Bankruptcy Act Sec. 39c) provides "a person aggrieved by an order of a Referee may . . . file with the Referee a petition for review of such order by a judge. . . ."

This section limits the right of review to a "person aggrieved," and such person must have a direct—not indirect—interest in the decision appealed from. (*Rogers v. Bank of America* (9 Cir.), 142 F. 2d 128, 129; *In re Henry Woods & Sons Co.,* 279 Fed. 608; *In re Realty Foundation,* 75 F. 2d 286, 287; 2 *Coll. on Bkcy.* (14th Ed.) 1479 *et seq.;* 8 *Rem. on Bkcy.* (6th Ed.) 292.)

In *Rogers v. Bank of America, supra,* this Court states:

> "The authority for instigating and maintaining the review of a referee's order by a judge under §39c is restrictive. It is granted only to those who have an immediate interest in the bankrupt estate, as such, and does not include those who would be indirectly affected by the order."

In re Camp Baking Co., 146 Fed. Supp. 935, 938, the Court defines a "person aggrieved" as one who has "a legal interest in the order sought to be reviewed."

It is well established that where trustee's interest in encumbered property is sold by Referee, subject to existing encumbrances, the mortgagees are not entitled to challenge or review an Order directing or confirming a sale of a bankrupt's equity in mortgaged property, subject to encumbrances, since, as creditors, they have no interest in preventing the sale, and as mortgagees, the sale cannot affect their security, or their remedy. A mortgagee is not a party aggrieved by such an Order, and his review therefrom will be dismissed.

In 8 *C. J. S.,* Bkcy., 1043 Par. 311b, the rule is thusly stated:

> ". . . encumbered property may be ordered sold subject to the encumbrances, leaving the lienholder to enforce his lien on the property by appropriate proceedings; mortgagees who are also general creditors are not entitled to challenge an Order directing the sale of the bankrupt's equity in mortgaged lands, since, as creditors, they have no interest in preventing the sale, and as mortgagees, the sale cannot affect their remedy." (See also 6 Rem. on Bkcy. (6th Ed.) 85 §2575.)

In re Huneston (2 Cir.), 83 F. 2d 187, 189, the Circuit Court dismissed an appeal from an Order which dismissed mortgagee's petition from Referee's Order which directed Trustee to sell encumbered personal property, subject to all liens. The Court states:

> "We cannot see by what warrant the mortgagees challenged the sale of the equity. It is true that they are general creditors, as well as lienors, but as creditors, they can have no interest in preventing a sale; and as mortgagees, it cannot affect their remedy in any way whatsoever."

In re North Star Ice & Coal Co., 252 Fed. 301, upon mortgagee's review of Referee's Order directing sale of bankrupt property subject to encumbrances, the Court states:

> ". . . the Referee found . . . that it was advantageous to unsecured creditors to sell . . . property of the bankrupt . . . subject to all valid encumbrances. . . . The trustee was not directed to sell anything except the bankrupt's interest. *No rights of the mortgagee were affected or impaired,* and, as it stood solely in the position of a secured creditor asserting a valid lien upon the property . . . *I am of the opinion that it has no standing to revise the Order of the Referee,* which will accordingly be confirmed." (Italics ours.)

In re Burr Mfg. & Supply Co., 217 Fed. 16, 19, 20, upon appeal from Order setting aside sale subject to encumbrances, upon review by mortgagee, the Circuit Court reversed said Order and reinstated the sale, stating:

> "Any person interested may apply to have the judicial sale vacated, unless by his actions, or his laches, he has become estopped. *But, he must be a party who is interested and injuriously affected by the sale.* (Citations.) *The mortgagees are without interest, because the Order confirming the sale was upon condition that the purchaser, Porter, should 'accept title subject to such, if any, liens as may be on the property.'"* (Italics ours.)

In *Smith v. McKenna Brass Mfg. Co.* (3d Cir.), 98 F. 2d 537, the Circuit Court held that a mortgagee cannot object to Trustee's sale of property sold subject to a mortgage, stating:

> "Here the Trustee sold 'such right, title and interest' as the bankrupt had in the property . . . and the appellant not being injured by the sale, *for the lien*

of his mortgage not being affected, he cannot now be heard to object." (Italics ours.)

In *Gotkin v. Korn,* 182 F. 2d 380, in discussing a sale of chattels, subject to liens, the Circuit Court stated:

> "It is perfectly clear, however, that where as here, the Bankruptcy Court chose to sell encumbered property subject to liens, it elects to sell only the bankrupt's equity therein, and so, in effect, *declines to exercise its exclusive power to deal with liens and relegates the holders to the enforcement remedies which would have been available to them had the lienee's bankruptcy not occurred."* (Italics ours.)

In *Bradley v. Williams,* 202 S. W. 2d 149, the Court of Appeals of Kentucky, in referring to a sale in bankruptcy, subject to encumbrances, states: "It passed title to an equity. It neither hurt nor helped any lienholder."

Furthermore, Sterett, who filed a secured claim [R. 21-29] without waiving her security [R. 22], and who petitioned for review, *as a secured creditor, was without interest in the proceeds of the sale of the personalty sold "subject to all chattel mortgages."*

Where property of a bankrupt is sold subject to encumbrances, one having a lien thereon must look to the property alone for payment, and cannot claim payment out of the proceeds of such sale. (8 *C. J. S., Bankruptcy,* 1066, Sec. 322c; *In re Gerry,* 112 Fed. 957, 958; *In re Klapholz,* 113 Fed. 1002, 1003.)

It is crystal clear that Millie Sterett was not a "person aggrieved" by Referee's Order Confirming Sale. The Referee's Certificate so states [R. 118-121]. Her Petition for Review should have been dismissed without relief. The challenged portion of the Order on Review clearly is erroneous.

II.

The District Court, Upon Review, Prejudicially Erred in Ordering Appellant to Release Its Chattel Mortgage Through Escrow to Appellee in That Appellee Was Estopped From Reviewing the Referee's Order, for Failing to Make Timely Objection Thereto, Where, Appellee, After Notice, Was Not Present at, and Did Not Participate in the Sale, and Made No Objection to the Bid, or Sale, or to Its Confirmation, at Any Time Prior to Confirmation.

Millie Sterett was given notice of the sale [R. 110, 119, 122 par. 5]. The Referee's Order so states [R. 68-69] and the District Court's Order so recites [R. 132-133]. She was neither present on September 6, 1957, nor participated in the sale, and made no objection to the bid of or sale to S. Kohn thereat, or thereafter, or to its confirmation at any time prior to Referee's Order Confirming Sale filed September 23, 1957. Under these circumstances, Sterett's objection to the Order by way of Petition for Review was not timely, and she was estopped from reviewing the same.

It is now settled that the right of Petition for Review may be lost by estoppel. The concept is that one who has been accorded due notice of contemplated action, but who fails to put in an appearance, or be represented before a Referee, should not have a chance, by afterthought, to upset what has transpired. This is based upon logic, and the necessities of progress in the administration of justice. (8 *Rem. on Bkcy.* (6th Ed.), 294; 2 *Coll. on Bkcy.* (14th Ed.), 1480; *In re Rose* (9th Cir.), 86 F. 2d 69-71; *In re Peppers Fruit Co.,* 24 Fed. Supp. 119, 121, 122 (D. C. Cal.); *In re Mifflinburg Body Co.,* 54 Fed. Supp. 560-561.)

2 *Coll. on Bkcy.* (14th Ed.), 1480, states:

> "Where matters are thus heard upon notice, reviews of order are limited to applications by parties who have appeared at the hearing before Referee, and participated therein."

The foregoing rule is succinctly stated in *In re Peppers,* 24 Fed. Supp. 119, 121-122, wherein the California District Court states:

> "This court feels that, in the interest of economy and efficiency of administration of bankrupt estates, reviews from referee's orders, at least those orders which are made after notice, should be limited to applications by parties who have appeared at the hearing before the referee and participated therein. Any other holding would leave the door open to a flood of reviews which would result not only in delay and expense, but would place an almost intolerable burden upon the district judges."

In *In re Mifflinburg Body Co., supra,* the Court states:

> "The reason for this rule is clear. When a party to litigation receives notice that a matter will be heard, it is his duty to appear at the hearing and present to the court evidence and legal authorities which will be of aid to the court in making its decision. If he does not do so, the court must make its decision without the benefit of any evidence which such person might have made available, and the court must act upon the presumption that persons who are absent are not interested in the matter before it, or will be satisfied with such decision as the court may make. To permit persons who did not participate in proceedings of which they are on notice to complain of the result of such proceedings would cause unlimited confusion and even disrespect of the courts and their authority."

This Honorable Court has applied a similar rule in respect to appeals in *In re Rose* (9th Cir.), 86 F. 2d 69, 71.

Sterett not only did not appear at or participate in the sale before the Referee, but also did not object or except to the bid, sale, or its confirmation at any time prior to the Referee's Order Confirming Sale signed and filed seventeen days after the sale [R. 117].

It is also well established that anyone who desires to file objections to a sale should do so immediately, as objections are too late after confirmation. (6 *Rem. on Bkcy.* 43; *In re Shamokin Lumber and Const. Co.,* 54 Fed. Supp. 480, 481; 4 *Coll. on Bkcy.* (14th Ed.) 1579, *et seq.*)

Where no objections are filed to a sale prior to its confirmation, a Petition for Review to review the Order of Confirmation will be dismissed. (*In re Shamokin,* 54 Fed. Supp. 480, 481.) The reason for this is that judicial sales are an indispensable part of the machinery employed in administering bankrupt estates. Public policy requires that nothing be done to impair confidence in stability of judicial sales. (*In re Strunk Lane v. Jellico, etc., Co., Inc.,* 64 Fed. Supp. 731, 733; *In re Winthrop Mills,* 109 Fed. Supp. 323, 325; *Pewabic Mining Co. v. Mason,* 145 U. S. 249, 256; 36 *L. Ed.* 732.) After confirmation, such sale can only be set aside for the same reasons which equity would set aside a sale between private individuals. (*Dyar v. Stewart,* 123 F. 2d 278, 280; *In re Burr Mfg. Supply Co.,* 217 Fed. 16, 17; *In re Pneumatic Tube Steam Splicer Co.,* 80 F. 2d 524; 4 *Coll. on Bkcy.* (14th Ed.) 1586.)

Millie Sterett, who did not appear at or participate in the sale and made no objection thereto prior to its confirmation, ought not to have been permitted to sit back, and *by review,* take "pot shots" at the sale and its confirmation, particularly on grounds never urged or presented before the Referee. The law does not countenance such action.

The District Court should have dismissed the Sterett Petition for Review with relief. The challenged portion of its Order is clearly erroneous.

III.

The District Court Upon Review, Prejudicially Erred in Ordering Appellant to Release Its Chattel Mortgage to Appellee in That Appellee's Petition for Review Contained No Ground for Review, or Specification of Error Challenging Referee's Order Upon the Claim That the Sale to S. Kohn Satisfied and Extinguished Appellant's Lien Claim and Chattel Mortgage. Such Claim Was First Asserted in the "Memorandum of Law" Filed at the Review Hearing, Which Could Not Enlarge the Scope of the Petition.

No ground of review, or specification of error is set forth in Sterett's Petition for Review [R. 75-81], which challenged the correctness of the Referee's Order upon the ground that the bid of and sale to S. Kohn satisfied and extinguished the Rosehedge lien claim and its chattel mortgage, or that any such question was presented to or determined by the Referee in his Order. Neither does her specification of insufficient evidence include any such specification or claim [R. 77-78]. Such assertion was first urged in Sterett's "Memorandum of Law" served and filed at the Review Hearing [R. 124-126]. The District Court prejudicially erred in considering such argument and in granting the requested relief.

U.S.C.A., Title 11, Section 67c (Bankruptcy Act 39c), requires that the Petition for Review must "set forth the Order complained of and the alleged errors in respect thereto." The Petition must be reasonably clear and specific as to the errors charged. Errors of law should be assigned by setting forth the rule of law applied by the Referee, and stating the correct rule as contended by Peti-

tioner. A petition which merely alleges errors in general terms is insufficient. The reviewing Court is not required to search the Record to discover the issues sought to be raised or questions presented. (8 *Rem. on Bkcy.* (6th Ed.) 304; 2 *Coll. on Bkcy.* (14th Ed.) 1488-1489; *In re Casaudoumesq,* 46 Fed. Supp. 718, 725 (D. C. Cal.); *In re Moskowitz,* 63 Fed. Supp. 1000; *In re Ainsworth,* 5 Fed. Supp. 523, 524.)

The Petition on Review cannot be enlarged or aided by counsel's "Memorandum of Law" or briefs on file (*In re Ainsworth,* 5 Fed. Supp. 523, 524); nor by argument or statements of counsel not supported by the record (*In re Paley,* 26 Fed. Supp. 952).

An assignment of insufficiency of the evidence, without showing how it fails to support the Order is insufficient upon the grounds not specified. (*In re Musgrove,* 27 Fed. Supp. 341, 342.)

The District Judge should not pass upon errors not specifically designated, and should dismiss the petition, as the Bankruptcy Act does not contemplate a general review of the proceedings had before the Referee, or of rulings not directly affected by the Order. (2 *Coll. on Bankruptcy* (14th Ed.) 1488-1489; *In re Moskowitz,* 63 Fed. Supp. 1000; *In re Casaudoumesq,* 46 Fed. Supp. 718, 725 (D. C. Cal.); *In re Kelly Dry Goods Co.,* 102 Fed. 747, 748.)

In re Kelly Dry Goods Co., supra, at 748, the Court, in discussing the scope of a review states that this does not mean "that a general review of the proceedings before the Referee, or review of rulings not directly affecting an Order made is intended by the Act or rules."

This is particularly applicable on review from an Order Confirming Sale for the District Judge does not exercise his general equitable powers, but acts analogous to an Appellate Court, in reviewing the decision of the referee upon

the petition before it—a petition which must be legally sufficient, and by a person having a legal interest in the matter. (*In re Realty Foundation, Inc.,* 75 F. 2d 286, 288; *In re Orpheum Circuit,* 24 Fed. Supp. 101, 104.)

In *In re Moskowitz,* 63 Fed. Supp. 1000, the Court in discussing the requirements of Section 39c of the Bankruptcy Act, stated that a general assignment of errors in the petition was insufficient to justify any consideration of the review, and that the failure of the petition for review to meet the requirements of Section 39c is sufficient, by itself, to cause a dismissal of the Petition.

A review based upon grounds different from those set forth in the Petition will be dismissed without reference to the merits of the case. (*In re Wyoming Valley Collieries Co.,* 29 Fed. Supp. 106, 108; *In re Loring,* 30 Fed. Supp. 758, 759.) A petition which urges a question not raised before the Referee will not be considered. (*In re Wachtel,* 64 Fed. Supp. 229, 239; *In re Bender Body Co.,* 47 Fed. Supp. 224.)

This Court has adopted a similar rule pertaining to specifications of error in appellate procedure, and have declined to pass upon points not specifically designated, or not presented to and passed upon by the trial court. (*Humphrey Gold Corp. v. Lewis* (9th Cir.), 90 F. 2d 896, 899.)

The various specifications of grounds for review in the Sterett Petition which were directed to Referee's Order dated September 6, 1957, constituted a collateral attack upon such Order and could not be considered. Her Petition for Review of Referee's Order dated September 23, 1957, was filed more than ten days after filing of the September 6, 1957, Order. (*In re Wyoming Valley Collieries Co.,* 29 Fed. Supp. 106, 108; U.S.C.A., Title 11, Sec. 67c; Bankruptcy Act, Sec. 39c.)

For each of the foregoing reasons, Sterett's Petition should have been dismissed without relief. The challenged portion of the District Court's Order is clearly erroneous.

IV.

The District Court on Review Prejudicially Erred in Ordering Appellant to Release Its Chattel Mortgage Through Escrow to Appellee, a Subsequent Mortgagee, Since Said Court, as a Bankruptcy Court Had No Jurisdiction to Determine the Rights and Priorities Between Appellant and Appellee Regarding Their Respective Chattel Mortgages Since the Property Had Been Sold "Subject to All Chattel Mortgages" and Neither the Trustee nor the Bankrupt Estates Were Involved or Had Any Interest in Such Controversy.

Millie Sterett's contention, *first* urged at the Review hearing—that the sale to S. Kohn satisfied the Rosehedge lien claim and extinguished its chattel mortgage, and that Rosehedge should be compelled to release its chattel mortgage [R. 124-126]—was a controversy between adverse third persons, Sterett and Rosehedge, regarding the rights and priorities of their respective chattel mortgages. Neither Trustee nor the Bankrupt Estates were interested therein. The personal property had been sold and confirmed to S. Kohn by Referee, "subject to all valid chattel mortgages" [R. 66-75]. The Bankruptcy Court thereby declined to exercise its exclusive power to deal with liens and relegated the lien-holders to their enforcement remedies which they would have but for the intervention of bankruptcy. These liens were not affected or impaired by such sale. (8 *C.J.S., Bkcy.* 1043; 6 *Rem. on Bkcy* (5th Ed.) 85, §2575; *In re Huneston,* 83 F. 2d 187, 189; *In re North Star Ice and Coal Co.,* 252 Fed. 301; *In re Burr Mfg. & Supply Co.,* 217 Fed. 16 (1920); *Gotkin v. Korn,* 182 F. 2d 380.)

In *Gotkin v. Korn, supra,* the Circuit Court states:

> "It is perfectly clear, however, that where as here the bankruptcy court chose to sell encumbered prop-

erty subject to liens, it elects to sell only the bankruptcy equity therein, and so, in effect, declines to exercise its exclusive power to deal with liens *and relegates the holders to the enforcement remedies which would have been available to them had the lienee's bankruptcy not occurred.*" (Italics ours.)

Where property of a bankrupt is sold subject to encumbrances, one having a lien thereon must look to the property alone for payment, and cannot claim payment out of the proceeds of such sale. (8 *C.J.S., Bkcy.* 1066, §322(c); *In re Gerry,* 112 Fed. 957, 958; *In re Klapholz,* 113 Fed. 1002, 1003.)

A Court of Bankruptcy is a Court of limited jurisdiction, possessing only the jurisdiction and powers expressly or by necessary implication conferred by statute, and as such it does not have general plenary jurisdiction in equity, but is confined in the application of the rules and principles of equity to the jurisdiction conferred upon it by the provisions of the Bankruptcy Act. Such jurisdiction does not extend to determine controversies between adverse third parties in which neither the trustee nor the bankruptcy estate has an interest, and which are not strictly and properly part of the bankrrupcy proceedings. (8 *C.J.S., Bkcy,* 429, §21; *Evarts v. Eloy Gin Corp.* (9th Cir.), 204 F. 2d 712, 715; *Billings Credit Men's Assn. v. Bogert* (9th Cir.), 8 F. 2d 307, 309; *Smith v. Chase Nat'l Bank,* 84 F. 2d 608, 614-615; *In re Railroad Supply Co.,* 75 F. 2d 530, 532; *Central Hanover Bank & Trust Co. v. Kelby,* 132 F. 2d 873, 875; *Chauncey, et al. v. Dyke Bros.,* 119 Fed. 1, 3.)

In *Evarts v. Eloy Gin Corp., supra,* this Court states the rule succinctly as follows (p. 715):

"Courts of Bankruptcy are invested with 'such jurisdiction at law and in equity as will enable them to exercise original jurisdiction in bankruptcy pro-

ceedings.' Title 11, U.S.C.A., §11. However, the jurisdiction thus granted is not plenary equity jurisdiction. It is bankruptcy jurisdiction, limited to the express statutory authorizations. The equity jurisdiction conferred by the Act merely empowers the judge or referee in bankruptcy to employ the rules and principles of equity jurisprudence in the exercise of his bankruptcy jurisdiction. *Smith v. Chase Nat'l Bank,* 8 Cir., 1936, 84 F. 2d 608, 614; *Billings Credit Men's Ass'n v. Bogert,* 9 Cir., 1925, 5 F. 2d 307, 309; *Pepper v. Litton,* 1939, 308 U. S. 295, 304, 60 S. Ct. 238, 84 L. Ed. 281; 8 *C.J.S., Bankruptcy* §21. Thus appellant's invocation of the equity powers of the Bankruptcy Court is not sufficient to confer jurisdiction on the Bankruptcy Court of the issues raised here, in the absence of some statutory authority. See 8 Colliers on Bankruptcy, 14th Ed., §3.01."

In *Smith v. Chase Nat'l Bank, supra,* the Circuit Court states at page 615:

> "The jurisdiction of the District Court, as granted by the Bankruptcy Act, is unquestionable bankrupt jurisdiction, and not general jurisdiction to hear and determine controversies between adverse third parties, which are not strictly and properly a part of the bankruptcy proceedings."

In *In re Railroad Supply Co., supra,* 532, the Court states:

> "It has generally been held that a Court of bankruptcy will not digress in the administration of a bankrupt estate to settle collateral disputes. Such a rule is obviously sound for its existence is to eliminate all extraneous issues from the bankruptcy proceedings and thus secure the early closing of the affairs of the bankrupt."

It is also well settled that where property is sold by a Referee, subject to liens, the lienholders have no interests in the proceeds of sale, and a Court of Bankruptcy has no jurisdiction to hear or determine controversies between adverse lienholders seeking to have their respective rights and priorities determined, merely because the claimants happen to be creditors of the bankruptcy estate, or merely because the liens affect a part of the bankrupt's property.

In 8 *C.J.S., Bkcy.* 926, the rule is stated thusly:

> "A bankruptcy court, however, has no jurisdiction to adjudicate controversy having no proper relation to the business with which it is entrusted, and it will not assume jurisdiction to determine rights or liens which in no way affect the collection of the assets, the administration of the estate, and the distribution of the assets."

In *Smith v. Chase Nat'l Bank,* 83 F. 2d 608, we find the following at 615:

> "In *Chauncy et al. v. Dyke Bros. et al.* (C.C.A. 8), 119 F. 1, 3, this Court speaking through Judge Thayer, said: *'The bankrupt court had no rights to assume jurisdiction of a controversy between third parties, in which the trustee was not concerned, and decide whose claim was paramount in equity, merely because the claimants happened to be creditors of the bankrupt estate, or merely because the liens affected a part of the bankrupt's property. The bankrupt act confers no such authority.'"* (Italics ours.)

Chauncey et al. v. Dyke Bros. 119 Fed 1, 3 (wherein the aforesaid rule was stated, but the Court assumed jurisdiction because the lienholders would have an interest in the sales proceeds).

In *Tuck v. Patterson,* 60 S. W. 2d 328; 29 A. B. R. (N. S.) 88, an attempt was made by adverse third parties,

to impose a trust in property sold by the Bankruptcy Court, and it was urged that such Court had jurisdiction to determine such controversy. The Court states:

> "The remedy would *not* require an *avoidance* of the conveyance made by the trustee nor reclamation of the land. *To the bankruptcy court belonged the power to make sale of the land of the bankrupt estate and to confirm the grant to the purchaser. The very subject-matter of its jurisdiction is the disposition and distribution of the bankrupt's estate. The jurisdiction of the bankruptcy court, however, is exhausted and it loses its absolute power upon the sale and confirmation of the sale of the land. In the sale and disposition of the land there is complete and effectual execution of the powers given to the bankruptcy court of administration upon the land.*" (Italics ours.)

Likewise, in the instant case, a determination of Sterett's claim that the S. Kohn bid and sale had extinguished the Rosehedge chattel mortgage *did not require the avoidance* of the sale or transfer of the property by the Trustee to S. Kohn. Such issue was totally *collateral to the sale* of the property, and to the bankruptcy proceedings.

It is well settled that where an Order of the Bankruptcy Court is partly within and partly without the Court's jurisdiction, the part without the jurisdiction *is void.* (*U. S. ex rel. Emanuel v. Jaeger,* 117 F. 2d 483.) The Court therein states, ". . . Where an Order is partly within and partly without the Court's jurisdiction, the part without is void."

The part without the jurisdiction is *coram non judice.* Like a dead limb upon a living tree, the void portion of the Order may be severed from the valid part without impairing the validity of the remaining portion of the Order.

A controversy between lien claimants as to their respective rights, particularly where the property is sold "subject to liens," should be determined by appropriate proceedings in a State Court, since such issues are governed by State laws. (*In re Kernick Divide Mining Co.,* 3 Fed. Supp.. 323 (D. C. Nev.); *Gotkin v. Korn,* 182 F. 2d 380.)

In the instant case, Sterett, upon Review, requested the District Court to determine that her chattel mortgage was paramount to Rosehedge's chattel mortgage as a result of the sale to S. Kohn. Neither the Trustee, nor Bankruptcy Estates had any interest in such controversy since the property had been sold "subject to all valid chattel mortgages." This controversy was one *solely* between Sterett and Rosehedge. The District Court, as a Court of Bankruptcy, *could not exercise its broad general equitable jurisdiction* to adjust the equities between those parties. Sterett in her "Memoranda of Law" [R. 124-126] claims that she was aggrieved by Referee's Order Confirming Sale *because Rosehedge refused to release its chattel mortgage* [R. 125]. A clearer example of a controversy between adverse third parties wherein neither the Bankrupt Estate nor the Trustee have any interest cannot be found, and the Bankruptcy Court would have no jurisdiction to determine such controversy. That portion of the District Court's Order ordering Rosehedge to release its chattel mortgage through escrow to Sterett, a subsequent mortgagee, is clearly without its jurisdiction, and is void. It should be stricken from the Order.

V.

The District Court Upon Review Prejudicially Erred in Ordering Appellant to Release Its Chattel Mortgage Through Escrow, as Such Portion of Its Order Is Not Supported by the Evidence in That There Is No Evidence That Appellant's Lien Claim and Chattel Mortgage Was Satisfied and Extinguished by the Bid and Sale.

The evidence upon this subject, with appropriate references to the record, is fully discussed and set forth under appellant's Specification of Error No. 8. To avoid unnecessary duplication, we respectfully make the same a part hereof by reference.

Briefly this evidence shows that the written bid made by S. Kohn [R. 29-33, 110-112]; the acceptance of said bid by the Referee, *as made* [R. 110-112, 116, 120-121]; and Referee's Order Confirming Sale [R. 66-74] *without contradiction,* that the property was sold to S. Kohn for $116,000.00 cash, the real property, subject to certain liens, including the Rosehedge lien and lien claim, and Trustee's interest in the personal property, subject to all valid chattel mortgages [R. 66-74]. The District Court's Order affirmed and confirmed the sale, *as made* by the Referee (excepting a modification of taxes) and expressly adjudicated that the real property was sold free and clear of all liens, except certain specified liens, *which included the Rosehedge lien and lien claim* [R. 134-135]. The purchase price was increased by $1,500.00 (to cover costs of preservation) to $117,500.00 *cash* [R. 130], but said property, nevertheless, was sold *subject to the aforesaid liens and chattel mortgages.*

On September 6, 1957, the Referee also adjudicated that LeRoy's secured lien claim was $272,722.50 [R. 37-38], and that Rosehedge's secured lien claim was $154,846.65, and on said date made and filed his Order thereon [R. 33-48].

The Referee's Order and the District Court's Order *do not recite, state, or find* that the bid of and sale to S. Kohn used or utilized the value of the LeRoy and Rosehedge claims, or either of them, or extinguished the Rosehedge chattel mortgage.

The proceedings had, and the statements made at the sale on September 6, 1957, as disclosed by Referee's Certificate [R. 110-116] *do not disclose,* any statement or announcement made or proceedings had at said sale which either announced or stated that the S. Kohn bid did, or was intended to, use, utilize, or include the value of the LeRoy and Rosehedge claims, or either of them. On the contrary, the announcement made, and the bid submitted at the sale, both oral and written, by S. Kohn, disclosed that S. Kohn offered to purchase the real property, *subject to specified certain liens* (including Rosehedge's lien) and Trustee's interest in the personal property *subject to all valid chattel mortgages,* and that this bid, *as made,* was *accepted* [R. 29-33, 111-112, 116], and *confirmed* [R. 64-74]. Neither Referee's summary of the evidence under Status of the Record [R. 121-123], or his The Questions Presented [R. 123] found in Referee's Certificate, contains any summary, statement, recital or finding that the S. Kohn bid and sale utilized or used the Rosehedge claim or extinguished its chattel mortgage, or that any such question was determined or presented.

The isolated portion of the Referee's Certificate set forth in Sterett's "Memorandum of Law" [R. 124-126] is insufficient *as a matter of fact and of law* to sustain the challenged portion of the District Court's Order [R. 117]. The Record contains nothing further on that subject. The statements in the extracted portion of Referee's Certificate were *not* made at the sale; they were *not* a part of the proceedings had thereat; the *sale had been completed* [R. 116]. This statement was *first made by Referee* in

Referee's Certificate on Review, *solely* for the purpose of *disproving* certain contentions urged on Review. But even the quoted statement [R. 124-126] fails to sustain Sterett's contention. It *discloses* [R. 117] that "This bid (S. Kohn bid) *was made subject to the liens and lien claims of LeRoy and Rosehedge";* it indicates that the bid *did not include or utilize the value of such claims,* for it states: "Had the bid been increased by the value of such lien claims, a credit upon the purchase price in the amount of the value of said lien claims would have had to be given," thus patently disclosing that the *actual bid made had not been increased by utilizing the value of the LeRoy and Rosehedge claims.* The expression "This, in the opinion of the Referee, at the time of sale was the equivalent of utilizing the value of the LeRoy and Rosehedge claims upon the bid made" *does not state that such values actually were used. It merely ilustrates that so far as the net result to the Bankrupt Estates, and the net amount of money received by the Trustee,* were concerned, the bid of S. Kohn was the *equivalent* of a bid which would have been increased by the value of the LeRoy and Rosehedge claims, for *if* such a bid had been made, a *credit* equal to the value of such lien claims would have had to have been given upon the purchase price, thereby *reducing* it to the *same net amount of cash actually received on the S. Kohn bid* [R. 120]. The Referee further, by way of illustration, showed that the S. Kohn bid *as made* (subject to specified liens and all chattel mortgages) was more beneficial to all creditors, than a free and clear bid would have been. He also stated that the S. Kohn bid and sale, *as made* (subject to liens and chattel mortgages), *in fact, did comply* with the provisions of the July 6, 1956, Order which also expressly provided for the sale of the real property "including . . . personal property . . . *upon such terms and conditions as the Court shall hereafter approve.*" The foregoing, *as a matter of fact,* discloses that the S. Kohn bid did not, and could not have

utilized the value of the LeRoy and Rosehedge claims. *As a matter of law,* Sterett's contentions cannot be sustained.

It is axiomatic that the Referee's Certificate, like any other judicial document, must be read and construed in its entirety, and isolated extracts therefrom must be read and construed with the other portions of the document. Furthermore, the language used must be read and construed *in the light of the facts and issues then before the Referee.* (21 *C.J.S.* Courts, 408, 412; *Porter v. Bakersfield,* 36 Cal. 2d 582, 590, 255 P. 2d 223.)

When the Referee made the statement relied upon by Sterett, and expressed his opinion therein, *there was no question or issue before him* whether the bid of and sale to S. Kohn *had utilized* the value of the Leroy and Rosehedge claims, and had extinguished Rosehedge's chattel mortgage. This contention *was first urged at the hearing upon Review,* and finds no basis in the Record.

The District Court, in reviewing a Referee's Order, is limited *to the record* before the Referee, and cannot accept arguments by or statements of counsel, as evidence. (*In re Paley,* 26 Fed. Supp. 952.) Evidence not taken or admitted before the Referee *cannot be considered on review.* (*In re Palmer Realty Corp.,* 54 Fed. Supp. 656.)

It is also well established that in a Bankruptcy sale, the Referee's Order Confirming Sale *is controlling and fixes the terms of sale and the rights and obligations of all parties.* (*In re Strand Theatre,* 109 Fed. Supp. 352; *In re Toledo Co.,* 152 F. 2d 210, 211; *American Dirigold Corp. v. Dirigold Metals Corp.,* 125 F. 2d 446, 454; *In re Rapier Sugar Feed Co.,* 13 Fed. Supp. 85, 89.)

Any *subsequent reasons, expressions, or statements for such Order cannot impeach the actual Order, as made,* for, as stated by the District Court, *In re Mercury Engineering Co.,* 60 Fed. Supp. 786, 788: *"The Referee speaks*

to the Court through his order which grants or denies certain things, and not through the reasons for the order." (Italics ours.)

General conclusions, or expressions of opinion by a Referee, unsupported by testimony, or excerpts therefrom, are insufficient to show a meritorious cause for review. (*In re Sadler,* 104 Fed. Supp. 886, 890; *In re Wachtel,* 64 Fed. Supp. 229, 230.)

The expression of opinion by the Referee that the bid of S. Kohn was the equivalent of utilizing the value of the Leroy and Rosehedge claim is *not a finding* that such values were used. Conclusions of a Referee are not, and cannot be used as findings of fact. (*In re Pioche,* 235 F. 2d 903; *In re Sadler,* 104 Fed. Supp. 886, 888; *In re Mercury Engineering Co.,* 60 Fed. Supp. 786, 788.)

Even if we *assumed* that such expressions of opinion by the Referee, as made in his Certificate on Review, *long after* the signing and filing of his Order, may be considered as "findings," *such "findings" cannot be used to impeach the Referee's Order, or to sustain the challenged portion of the District Court's Order on Review.*

It is well settled that a Referee *cannot make additional Findings of Fact after a Petition for Review is filed.* (*In re Peoria Braumeister Co.,* 138 F. 2d 520, 522; 8 *Rem. on Bkcy.* (6th Ed.) 310.)

In re Peoria Braumeister Co., supra, at 522, the rule is succinctly stated as follows:

> "[1, 2] First of all, feel constrained to express our view that it was improper for the referee to make additional findings of fact in his certificate after the petition for review had been filed. It should be noted that the referee made his order on April 2, 1942; that the appellant filed its petition for review on April 13, 1942; and that the additional

> findings . . . were made on September 24, 1942. Neither §39, sub. a(8) of the Bankruptcy Act, 11 U. S. C. A. §67, sub. c, which deals with the review of a referee's order, providing that the petition for review '* * * shall set forth the order complained of and the alleged orders in respect thereto,' contemplates that a referee may make additional findings of fact some five months after a petition for review has been filed. *Instead* §39, sub. c, *requires* that the petition for review set *forth the alleged errors committed by the referee. This is obviously impossible if the referee is allowed to make additional findings after the petition is filed."* (Italics ours.)

Where there are neither pleadings nor proof respecting an issue, a "finding" by the Referee on such matter will be disregarded. (*Matter of Pittsburgh—Big Muddy Coal Co.,* 215 Fed. 703, 706; 2 *Collier on Bkcy.* (14th Ed.) 1502.)

The fact that S. Kohn made the bid and sale in her name, but was acting on behalf of Leroy and Rosehedge *is not* sufficient to sustain the contention that such bid and sale satisfied the Rosehedge lien claim and extinguished its chattel mortgage, either as a matter of fact, or of law.

Merger of a lien with title, and extinguishment of a mortgage debt is a matter of intent, and this is *a question of fact.* It is well settled that a merger of lien, or a satisfaction of mortgage debt does not result from a conveyance of the equity of redemption to *an agent or trustee* of the mortgagee; where a mortgagee takes title in the name of another to hold in trust for the mortgagee, there *is no intent to merge the lien or satisfy the mortgage debt,* particularly so when the property is purchased and conveyed *"subject to encumbrances."*

Furthermore, the law is well settled that a merger of lien, and the extinguishment of a mortgage debt will

not result, where the rights of inferior lien claimants are involved; it will be presumed in such case that the mortgagee intended that which would best accord *with his own interest,* and that he did not intend to merge his lien and extinguish his debt for the benefit of an inferior lien claimant.

These and other well established principles of law, together with their applicable citations, *will be fully set forth in the* next succeeding point of this Brief, Point VI. To avoid unnecessary duplication, we respectfully direct the Court's attention to said Point VI for a full discussion of the law upon this subject.

The evidence herein is totally insufficient to sustain the challenged portion of the District Court's Order.

VI.

The District Court Upon Review, Prejudicially Erred in Holding That the Bid of and Sale to S. Kohn, Acting on Behalf of Appellant and Leroy, as a Matter of Law, Satisfied Appellant's Lien Claim, and Extinguished Its Chattel Mortgage in Favor of Appellee, a Subsequent Chattel Mortgagee.

A merger of lien and extinguishment of the mortgage debt is a *matter of intent and a question of fact;* a bid in the name of and a sale to a third person indicates no intent by a mortgagee to merge the lien and extinguish the debt, *particularly where the rights of inferior lien claimants intervene.*

The District Court on Review ruled, as a matter of law, upon the Record before it, that the bid of and sale to S. Kohn, satisfied Rosehedge's lien claim, and extinguished its chattel mortgage in favor of Sterett, an inferior chattel mortgagee; therefore, it ordered Rosehedge to release its chattel mortgage through escrow to Sterett.

That the evidence fails to sustain such ruling has been demonstrated under our preceding Point V. We will now show this ruling is incorrect *as a matter of law.* The only substantial evidence before the District Court was that the bid was by and in the name of S. Kohn, who was acting on behalf of Leroy and Rosehedge. [R. 110-111.] The property, however, was sold and confirmed by the Court to S. Kohn *subject to specified liens and all chattel mortgages* for $116,000.00 *cash* (on review increased to $117,500.00 to cover additional costs of preservation.)

To effectuate a merger, the *right* or *estate* previously held, and the right or estate subsequently acquired *must coalesce* in the *same* person, and in the *same right and capacity* without any *intervening* equity or right, and with the *intent* of such person to *merge* the *two* estates and *extinguish* the lesser one. (*In re May,* 10 Fed. Supp. 829, 831; *Walters v. Baer,* 50 F. 2d 995, 996-997; *Sheldon v. LaBrea,* 216 Cal. 686, 690, 15 P. 2d 1098; *Buell v. Simon Newmark,* 61 Fed. Supp. 157-159.)

In order to effectuate a merger, the whole title, legal, as well as equitable, must unite in *one* and the *same* person in the *same capacity.* (*In re May,* 10 Fed. Supp. 829-831; *Walters v. Baer,* 50 F. 2d 995, 996; *Sheldon v. LaBrea,* 216 Cal. 686, 690, 15 P. 2d 1098; *Boye v. Voerner,* 12 Cal. App. 2d 186, 187, 54 P. 2d 1116.)

A recital in a deed, or other instrument, that the property is acquired subject to liens, encumbrances, or chattel mortgages, *shows no intent* to extinguish the lien and mortgage debt, and there can be no merger of either the lien or the extinguishment of the mortgage debt. (*Anglo-California Bank v. Field,* 146 Cal. 644, 652-653, 80 Pac. 1080; *Philadelphia Savings Fund Society v. Stern,* 23 A. 2d 413, 243 Pa. 534; *Monheit v. Cigna,* 28 Cal. 2d 19, 25, 168 P. 2d 965.)

Mergers of liens are *not* favored in law. The question whether a conveyance constitutes a merger of lien, and extinguishes the mortgage debt is a question of intent—the *mortgagee's intent,* who has the *election in equity* to prevent the merger and keep the mortgage alive.

In 59 *C.J.S.* Mortgages 677, we find the following:

> "The question whether a conveyance of the equity to the mortgagee results in a merger of the mortgage and fee is primarily one of intention of the parties, particularly, according to the decisions on the question, the intention of the mortgagee, for the mortgagee has an election in equity to prevent a merger and keep the mortgage alive." (To same effect: *Toston v. Utah Mortgage Loan Corp.,* 115 F. 2d 560, 562; *Guaranty Trust Company of N. Y. v. Minneapolis & St. L. Ry. Co.,* 36 F. 2d 747, 764.)

Such intent is a question of fact. (*Hines v. Ward,* 121 Cal. 115, 118, 53 Pac. 427.)

It is well established that a merger does *not* result from the conveyance or transfer of the equity or redemption *to an agent or trustee of the mortgagee.* An intent not to effectuate a merger is indicated where the mortgage is referred to as an existing lien, and when the mortgagee takes title in the name of another, either as agent of, or trustee for the mortgagee.

In 59 *C.J.S.,* p. 674, it states:

> "A merger does not result from the conveyance of the equity of redemption to an agent of the mortgagee. . . ."

On page 680 of the same volume, we find:

> "On the other hand, an intent not to effectuate a merger is indicated where the mortgage is referred to as a subsisting lien in the deed to the mortgagee . . . or where the mortgagee takes title *in the*

name of another, or where such other takes title to hold in trust for the mortgagee. . . ." (Italics ours.) (To same effect: *Humrich v. Dalzell,* 166 Atl. 511, 512, 113 N. J. Eq. 310; *Knowles v. Older,* 220 N. W. 625, 57 N. D. 128; *Knowles v. Tuttle,* 220 N. W. 623, 57 N. D. 138; *Hamilton v. Riddell,* 60 S. W. 2d 881; 41 C.J. 778; *Silverstein v. Saster,* 189 N. E. 540, 285 Mass. 453; *Barber v. Hartley,* 298 Pac. 226, 136 Ore. 210.)

In *Humrich v. Dalzell, supra,* the facts are almost identical with the instant case. In a foreclosure action, the defendants claimed "a merger of the legal title with equitable title under the mortgage and satisfaction or extinguishment of the debt secured by the mortgage." The property had been conveyed to one Mary T. McCartney "subject to all liens and encumbrances" who was a secretary of Complainants' solicitor. She, in turn, conveyed the property to Complainant's son "subject to all encumbrances of record." It was conceded that Mary T. McCartney took title as the nominee and agent of Complainant, who paid the consideration for the conveyance, and that property was conveyed to Complainant's son "as the agent for the Complainant." In rejecting defendant's claims of merger and extinguishment, the court states (p. 512):

> "[I] Merger is not favored in equity, and is never allowed, unless for special reasons and to promote the intention of the party, and, where equities are subserved by keeping the mortgage alive, and no injury is thereby wrought, it is not extinguished. (Citation.) The conveyance of the fee to a mortgagee will not merge his mortgage, where such intention on his part does not exist. (Citation.) The controlling fact in all instances is the intention of the person in whom the respective interests are united. . . .

"In the instant case, the evidence documentary and oral leaves no doubt that the complainants intended that the mortgage should not merge. It was the complainant Frank Humrich's testimony . . . that he arranged to have the conveyance made to Miss McCartney, the secretary to Mr. Edward S. Atwater, Jr., who was complainants' solicitor at that time to protect his interest in the same. . . .

" 'The fact that Humrich advanced the $200 for the purchase of the equity of redemption and obtained it to be conveyed to another to hold for his benefit is evidence that there was no intention to merge the equity of redemption with the mortgage, and it will not be held to have merged.' (Citations.) *'Merger does not result from the conveyance of the equity of redemption to an agent of the mortgagee.* 41 Corpus Juris, §880, p. 783.' " (Italics ours.)

In *Barber v. Hartley, supra,* the Court states:

"No principle is better settled than a mortgagee purchasing an equity of redemption *preserves his mortgage unmerged by taking a conveyance to a trustee."* (Italics ours.)

In *Knowles v. Tuttle, supra, Knowles v. Older, supra,* and *Hamilton v. Riddel, supra,* the conveyances were taken in the name of the spouses of the mortgagee. In each of said cases, it was held that taking title to the property *in the name of a third person evidenced an intent not to merge the lien or extinguish the mortgage indebtedness, and that no merger resulted.*

In the instant case, the Sterett chattel mortgage was subsequent and inferior to the Rosehedge chattel mortgage. [R. 10-12.] This was conceded. [R. 124.] The Trustee's interest in the personal property was purchased

"subject to all valid and subsisting sales contracts and chattel mortgages against the personal property." Obviously Rosehedge, for *its own interest and protection, would not merge* its chattel mortgage and extinguish its mortgage debt, *for the benefit of inferior chattel mortgagees.* The fact that the bid was made by *and in the name of S. Kohn,* and the sale was confirmed *in her name,* and the Trustee was ordered to convey and transfer the property to her, and in her name, subject to specified liens, and all chattel mortgages, indicates an intention *not to merge* the chattel mortgage lien, and *not to extinguish* the mortgage debt.

It is the *universal rule* that where there are intervening liens or rights, *it is presumed, as a matter of law,* that the mortgagee intends to *retain* his chattel mortgage and fully *protect* his mortgagee's *lien* and *rights,* and that *no merger* will be implied, or will result, *even where mortgagee takes title in his own name.* Equity will keep the legal title and mortgagee's interest *separate though they are held by the same person, whenever it is necessary for the full protection of mortgagee's interest.* The aforesaid rule applies when the intervening lien is a chattel mortgage. (33 Cal. Jur. 2d 672; 59 C.J.S. Mortgages 682, 683; *The Bergen,* 64 F. 2d 877.) Most certainly such a rule is applicable where legal title is taken in the name of, and held by, a *third person,* subject to all *chattel mortgages.*

The foregoing principle of law is applied and stated in the Ninth Circuit Court's own case of "The Bergen," 64 F. 2d 877. The Court states (pp. 880-881):

> "The majority rule is thus stated in 39 L. R. A. (N. S.) 839, note (b) (1): 'By the weight of

authority, a discharge by the mortgagee of his lien and the surrender of the evidence thereof to the mortgagor . . . does not operate as an extinguishment of the lien as against junior or intermediate encumbrances, and the senior lien still retains its priority. Different theories to sustain this doctrine are advanced by the cases, but with few exceptions they all reach this result.'

"In 41 C. J. 779, the following language is found: 'A merger will not be held to result wherever a denial of a merger is necessary to protect the interests of the mortgagee, the presumption being, in the absence of proof to the contrary, that he intended to do what would best accord with his interests. On this ground a merger has been denied even where the conveyance was admittedly made in satisfaction and cancellation of the indebtedness, or where the mortgagee took the conveyance under the mistaken belief that a merger would result but with no desire or agreement on his part to bring it about.' . . .

". . . the doctrine of merger, in the common law and in equity, in the latter it has been uniformly held that where an incumbrancer, by mortgage or otherwise, becomes the owner of the legal title or of the equity of redemption, *the merger will not be held to take place if it be apparent that it was not the intention of the owner, or if in the absence of any intention said merger was against his manifest interest.* . . .

"The rule in California is in harmony with that of the majority. In 18 Cal. Jur. §§390, 391, pp. 76, 77, the doctrine is thus stated: 'Indeed it is presumed as a matter of law that the party must have intended to keep on foot his mortgage title when it is essential to his security against an intervening title

> or for other purposes of security; and this presumption arises although the parties, through ignorance of such intervening title or through inadvertence, have actually discharged the mortgage and cancelled the notes with the intention to extinguish them.' " (Italics ours.)

Most certainly where the bid was made by, and in the *name* of S. Kohn, and *not* by, or *in the name* of Rosehedge, *subject to all chattel mortgages* [R. 29-33, 110-112, 116] and the Referee's Order confirmed said sale to S. Kohn "subject to all chattel mortgages" [R. 66-74, 73], and not to or in the name of Rosehedge, and Sterett had an inferior, intervening chattel mortgage, *the law would not presume that a merger was intended,* but on the contrary, *the law would presume that no merger was intended.* The District Court could not summarily decree, *as a matter of law,* on the Record before it, that a merger and extinguishment of the Rosehedge mortgage and mortgage debt took place, and thus order Rosehedge to release its chattel mortgage through escrow in favor of a subsequent inferior chattel mortgage. The law is directly to the contrary. The District Court prejudicially erred in ordering Rosehedge to release its chattel mortgage through escrow to Millie Sterett.

VII.

The Disitrict Court Upon Review Prejudicially Erred in Depriving Appellant of Its Day in Court Upon the Merits by Summarily Determining the Chattel Mortgage Rights and Priorities Between Appellant and Appellee, Where There Was No Pleading, No Notice of Hearing, or Hearing, or Presentation of Evidence Upon That Issue. Such Issue Was Properly Triable in Appropriate Proceedings in the State Court.

The District Court summarily determined the rights and priorities between Rosehedge and Sterett upon their respective chattel mortgages, upon the merits. Upon review from Referee's Order Confirming Sale, it neither had the right nor the power to do so. Those were matters for future determination in appropriate proceedings before the State Courts, as those issues were governed by State law. (*In re Kernick Divide Mining Co.,* 3 Fed. Supp. 323 (D. C. Nev.); *Gotkin v. Korn,* 182 F. 2d 380; 8 *C.J.S., Bkcy.* 936, 1043; *In re Westley Corp.,* 18 Fed. Supp. 347.)

In 8 *C.J.S.* 936, we find the following:

> "Where, however, the priority of conflicting liens depend upon the construction of State statutes, the question should be decided by appropriate proceedings in a State Court."

In re Kernick Divide Mining Co., supra, the District Court of Nevada, when confronted with the question of whether the Bankruptcy Court, or State Court should determine the question of priorities between lien claimants states:

> "Questions of this character ought, if possible, to be determined by the state courts for the reason that the federal courts are bound by the construction placed upon state statutes by the state courts, while

> the reverse is not the rule. A serious attack is also made against the decree in the Ward suit. The controversy between these two parties, especialy respecting validity, amount, and priority of lien, ought to be determined by appropriate proceedings in the state court."

Particularly is the foregoing rule applicable where the property is sold and confirmed by the Bankruptcy Court, *subject to encumbrances,* for in such sales the lien claimants cannot challenge or review such Order. (Points and Authorities, Point I of this Brief.)

Assuming, but not conceding, that the Bankruptcy Court had jurisdiction to determine the rights and priorities between Rosehedge and Sterett respecting their chattel mortgages, the challenged portion of the District Court's Order is clearly erroneous.

The Record discloses that while Sterett was given Notice of Sale [R. 68-69, 132, 133] she was neither present or represented thereat, nor objected to its confirmation at any time prior to the filing of Referee's Order Confirming Sale on September 23, 1957 [R. 110, 117]. No adversary, or other proceedings, between Rosehedge and Sterett, either at the sale or thereafter, was ever held before the Referee, involving any issue relating to their rights and priorities of their respective chattel mortgages, or upon the question whether the Rosehedge lien claim or its chattel mortgage were satisfied or extinguished in favor of Sterett by the S. Kohn bid and sale. Sterett's Petition on Review [R. 75-81] contains *no* grounds for review, and *no* specification of error challenging the Referee's Order upon such grounds, nor did it present any such question for or upon review. Such issue and question was *first raised by Sterett in her Memorandum of Law served and filed at the time of the Review hearing* [R. 124-126].

The Petition on Review cannot be enlarged or aided by briefs on file. (*In re Ainsworth,* 5 Fed. Supp. 523, 524.) No evidence upon that issue was presented either before the Referee or District Court.

The District Court, in reviewing a Referee's Order is *limited* to the Record before the Referee, and cannot accept arguments by, or statements of counsel as evidence. (*In re Paley,* 26 Fed. Supp. 952.) Evidence not taken or admitted before the Referee *cannot be considered.* (*In re Panamer Rlty. Corp.,* 54 Fed. Supp. 656.) Obviously no notice of hearing was given to appellant *upon those issues;* Appellant was never presented with *any pleading* upon those issues, nor was it given any notice of hearing, or any hearing, upon such issues. Those issues were *first raised at the hearing* [R. 124-126]. It is, therefore, crystal clear that the District Court, upon review, in summarily determining the rights and priorities between Rosehedge and Sterett deprived Rosehedge of its chattel mortgage, *without due process of law,* and by so doing it committed reversible error.

It is fundamental that a lienholder cannot be divested of his lien without notice and an opportunity to be heard and present evidence upon such issue in support of his claim and lien. (*In re Wachtel,* 64 Fed. Supp. 229; *Coates v. Maguire Oil and Ref. Corp.,* 47 Cal. App. 2d 275, 279, 117 P. 2d 898; 6 *Rem. on Bkcy.* (6th Ed.), 119, 120; *Sylvan Beach v. Koch,* 140 F. 2d 852, 861.)

The foregoing rule is succinctly stated in *Coates v. Maguire, supra* (p. 279), wherein the Appellate Court of California states:

> "Even if the bankrupt had been the mortgagor instead of the mortgagee and the mortgaged property had been possession of the bankrupt on adjudication, still the court *could not have affected the lien without notice and hearing to the lienholder.* . . . The reason

for the rule is obvious. *Nothing short of notice and hearing is due process, and due process is required in a bankruptcy court as well as in a court of general jurisdiction.* It is unnecessary to refer to the cases in the subject in detail, but see *In re De Fatta,* 10 F. Supp. 375; *In re Platteville Foundry & Machine Co.,* 147 F. 828; 7 C. J., sec. 307, note 33; 8 *C. J. S.* sec. 311, notes 81, 82." (Italics ours.)

In re Wachtel, supra, upon Trustee's Petition, and mortgagee's answer thereto, the Referee invalidated mortgagee's chattel mortgage, without any hearing or any presentation of evidence and based his ruling solely upon bankrupt's testimony at the first meeting of creditors. Upon review, this was reversed. The Court stated: "However, he (mortgagee) is entitled to a hearing at which witnesses are produced. Such a hearing should be had."

The Court in *Sylvan Beach v. Koch, supra,* states:

> "In the absence of (1) notice to a party of the claim made against him, and (2) of a hearing or an opportunity to be heard in opposition thereto, a judgment entered upon the claim is a nullity."

Since the question of merger of lien and extinguishment of mortgage debt is dependent upon the question of intent —the intent of the mortgagee—which not only is a question of law, *but also a question of fact,* Rosehedge was entitled to be served with pleadings properly presenting those issues and with notice of hearing, and given an opportunity to be heard and to present its evidence, and the law upon such issue. No such pleadings, notice, hearing, or opportunity was accorded it. The summary determination by the District Court on Review, *as a matter of law,* clearly is erroneous. It not only deprived appellant Rosehedge of its chattel mortgage lien without due process of law, but the District Court was without authority to

determine such issue, particularly upon a Review, which did not include or cover such issue.

The challenged portion of the District Court's Order is clearly erroneous, and should be reversed, and stricken from the other portions of said Order.

Conclusion.

We respectfully submit that the Record is replete with prejudicial reversible error which materially affects Appellant to its prejudice. We, therefore, respectfully submit that that certain portion of the District Court's Order, from which Appellant has appealed, and which is more particularly set forth in its Notice of Appeal [R. 139-141] and on pages 1 and 2 of this Brief, should be reversed, and such portion should be stricken from said District Court's Order, and that Appellant recover its costs of appeal herein.

Respectfully submitted,

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